Dissenting Report by Government Senators

1.1 While the majority report of the Committee contains some informative discussion of some elements of the Commonwealth Government's Asset Recycling Initiative, it provides an unbalanced presentation of the evidence and arguments received during the course of the inquiry. A number of the issues raised by participants to the inquiry highlight some of the benefits of the Government's asset recycling policy as well as evidence on the wider benefits from infrastructure privatisation were not considered or only received limited attention. This imbalance has resulted in recommendations of the majority report that are either unnecessary — as they call for processes or actions for which there are already established mechanisms within governments — or misguided, and hence cannot be supported.

Importance of Infrastructure to Economic Growth

1.2 Spending on productivity enhancing infrastructure is one of the keys to economic growth and prosperity. The Government is responding to the needs of the economy by building infrastructure that will drive economic growth, create jobs and improve productivity:

1.3 A core element of the Government's Economic Action Strategy is the commitment of an additional $11.6 billion for the Infrastructure Growth Package. Part of the 2014–15 Budget, the Growth Package delivered $5 billion for the Asset Recycling Initiative, $3.7 billion to boost infrastructure investments to expenditure projects and $2.9 billion for the Western Sydney Infrastructure Plan. The Commonwealth's total investment in infrastructure through to 2019–20 will be around $50 billion.

1.4 This investment will generate significant additional state and private sector participation to build the infrastructure that Australia needs and will transform infrastructure across the country to lay the foundations for future growth. When the construction projects supported by the Government's infrastructure initiatives are completed, they will add around 1 percentage point to GDP.

Asset Recycling Initiative

1.5 The Asset Recycling Initiative is designed to provide incentives to States and Territories to realise existing assets (sale or lease) and invest the proceeds in new, productivity enhancing infrastructure. This 'recycling' frees money currently locked up to help fund the projects that the States and Territories consider important to their future economic prosperity. The Initiative taps into private sector investment interest in current assets in order to fund new infrastructure.

1.6 The Commonwealth will provide incentive payments to the States and Territories of 15 per cent of the sale price of assets, but only on the condition that proceeds are reinvested in productivity enhancing assets. The initiative is estimated to support up to $38 billion in new infrastructure spending according to the Department of Infrastructure and Regional Development.[1]

1.7 The first Asset Recycling Initiative agreement was signed with the Labor Government of the ACT on 19 February 2015 – around $60 million in incentive payments following the ACT's decision to sell ACTTAB along with some property assets.

1.8 On 8 March 2015 the Commonwealth Government announced $2 billion in incentive payments for crucial infrastructure projects in conjunction with the NSW State Government.[2]

Privatisations under previous governments

1.9 In addition to placing heavy reliance on the views of union witnesses, the committee majority has placed a very heavy reliance in their report on testimony from Mr Stephen Koukoulas, quoting him at length. Mr Kouloulas was an economic adviser to the former Labor Government, serving as Senior Economic Adviser to Prime Minister Julia Gillard from September 2010 to July 2011.[3] It is not very convincing for the Labor majority to place heavy reliance on the opinions of a former Federal Labor adviser in support of the Federal Labor prejudice against privatisation.

1.10 The former Labor Government presided over a period when privatisations at a federal level were dormant, because of the economic prejudices of that Government. The former Hawke and Keating Labor Governments were far more reformist and modern in their outlook, undertaking a series of privatisations across different points in the economic cycle (see Table 1 below). In contrast to the Rudd/Gillard/Rudd Labor Government's record, state Labor governments have also pursued a number of privatisations including several that straddled the same period (see Table 2 below).

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1 Department of Infrastructure and Regional Development, *The Asset Recycling Initiative*, http://investment.infrastructure.gov.au/publications/reports/pdf/factsheets2014/Factsheet_The_Asset_Recycling_Initiative.pdf, (accessed 5 March 2015).

2 The Hon Joe Hockey MP, Media release, *$2 billion Asset Recycling deal to rebuild NSW*, http://jbh.ministers.treasury.gov.au/media-release/016-2015/, (accessed 18 March 2015).

3 Stephen Koukoulas, http://www.marketeconomics.com.au/stephen-koukoulas, (accessed 18 March 2015).

Table 1: Commonwealth Privatisations under Labor

Commonwealth Privatisations under Labor	Sale Proceeds ($m)	Government
April 1988 Commonwealth Accommodation and Catering Services	14.9	Hawke
November 1988 Defence Service House Corporation Loan Portfolio	1,515	Hawke
May 1991 Australian Defence Force Home Loan Franchise	42	Hawke
June 1991 Commonwealth Housing Loan Assistance Schemes in the ACT	47.3	Hawke
September 1992 Australian Airlines	400	Keating
March 1993 25% of Qantas	665	Keating
October 1993 Commonwealth Bank Secondary Public Share Offer	1,700	Keating
November 1993 Snowy Mountains Engineering Corporation	1.5	Keating
June 1994 Moomba-Sydney Pipeline System	534	Keating
June 1994 CSL (former Commonwealth Serum Laboratories) Public Share Offer	300	Keating
June 1994 Commonwealth Uranium Stockpile	57	Keating
June 1995 Aerospace Technologies of Australia Pty Ltd	40	Keating
July 1995 Qantas Public Share Offer	1,400	Keating

Table 2: Privatisations under state Labor governments

Year	State	Asset	Price ($m)	Government
1994	Queensland	Gladstone Power Station	750	Goss (ALP)
1997	NSW	NSW TAB	936	Carr (ALP)
1999	Queensland	Queensland TAB	268	Beattie (ALP)
2006	NSW	DirectLink	170	Iemma (ALP)
2006	Queensland	Allgas Energy	535	Beattie/Bligh (ALP)
2006	Queensland	Sun Retail	1,202	Beattie/Bligh (ALP)
2007	Queensland	Powerdirect	1,200	Beattie/Bligh (ALP)
2010	Queensland	QR National 66% sale	4,050	Bligh (ALP)
2010	NSW	NSW Lotteries	1011	Rees/Keneally (ALP)
2010	NSW	First tranche of electricity assets	5,300	Keneally (ALP)

Income substitution effects

1.11 In their report, the committee majority claims that privatisation of an income producing business would cause a state or territory government to lose dividend streams, as well as tax equivalent payments under the National Tax Equivalence Regime.

1.12 This argument simply ignores that the cessation of future dividend flows would be compensated through capital proceeds from sale (which implicitly recognise long-run income producing potential, net of holding costs and other factors affecting the value of the business in question).

1.13 It also ignores the fact that direct dividends to taxpayers through a state or territory government would be replaced in future with corporate income tax and income tax from resident shareholders who receive dividend streams. While these tax streams would flow to the Commonwealth following privatisation, the 15 per cent incentive provides an up-front incentive to partly recognise the movement of benefits between tiers of government. Far from the incentive “distorting” decisions, as the majority contend, it helps make the decisions stand more clearly on their merits by removing a current disincentive to privatisation.

1.14 Government Business Enterprises face inherent difficulties in doing their job well and it is these problems that have impelled governments to increasingly look at alternative forms of delivery, such as privatisation.

1.15 Government run business operations have found it increasingly difficult to obtain funding injections from Government because they have to compete against other high priority pressures for taxpayer spending. As a result Government Business Enterprises can be prevented from or hamstrung in the extent to which they can upgrade new plant and equipment or invest in business innovation or re-engineering (eg: modern IT or improved business processes). As a result, while these business operations are in public hands, the value creating capacity of these operations can be constrained. Private operators in practice have better flexibility to access capital and improve business efficiency and output. This means that private control and investment can also maximise the profitability of such business operations and the tax yield which flows back into public hands.

Evidence about specific privatisations

1.16 The committee majority has placed an unusual level of reliance on examples from the Northern Territory, citing testimony from the Northern Territory Labor Party and trade union officials. Curiously the committee has not taken any interest in the privatisation proposals announced by the Australian Capital Territory. The ACT Labor Government became the first administration to sign up to a privatisation program under the Australian Government's Asset Recycling Initiative.

1.17 The committee majority also ignored the recent Medibank Private sale, which is an exemplary case of a privatisation done well and is a key part of the Asset Recycling Initiative. This is one of the largest floats in Australian history. This sale provides $5.679 billion in proceeds that will be re-invested into productivity enhancing infrastructure through the Government's Asset Recycling Initiative.

1.18 The committee majority has floated some short-sighted testimony from particular opponents of privatisation. Mr David Richardson of the left-wing Australia Institute argued that privatisation sometimes requires an investment by taxpayers in improving the regulatory oversight of an industry, where previously there was inadequate supervision to protect consumer interests. This view overlooks the fact that continued public ownership of a business operation can place the Government in a conflicted position, as both regulator and provider of services. That conflict can work against the interests of consumers and business. The desirability of sound regulation does not disappear where a Government operator is a participant in the market.

1.19 The committee majority contradicts itself where it subsequently stresses the importance of good regulation, to ensure fairness in competition and to give certainty to the operators in a market ahead of privatisation. The arguments for good regulation and for safeguards against anti-competitive behaviour are not exclusively applicable to privatisation, but equally well apply to Government monopolies.

Impacts of infrastructure privatisation on consumers and capital productivity

1.20 An unfortunate result of the majority report's selective use of evidence is that considerable relevant information and evidence available was ignored or received limited consideration. For example, there is substantial evidence that privatisation of infrastructure tends to lead to reduced prices to consumers and more productive use of infrastructure assets. The improved outcomes in terms of prices are likely to reflect several factors. Governments that own infrastructure face mixed incentives, particularly as higher prices can assist with budget bottom lines. Privatised operations generally face higher incentives for efficiency. This has been confirmed in a number of studies, including several released during the final months of the inquiry.

- A report by Ernst and Young, prepared for Infrastructure Partnerships Australia concluded that in privatised networks businesses generally operate more efficiently, resulting in lower price increases.[4] These results were achieved without compromising service standards, and applied across both urban and rural customers.
- An Australian Industry (AI) Group report released in January concluded overinvestment in the network over time had substantially increased the state's electricity prices.[5] The report found that Queensland's electricity prices could be expected to fall substantially if power companies were privatised. Another benefit of privatisation identified in the report was the capacity to free up capital for reinvestment.
- A report by CME commissioned by UnitingCare on electricity prices released in February 2015 showed how costs to Victorian consumers, specifically network charges, were about half those in the Queensland and NSW level.[6] Further, the privatised Victorian system has seen network charges also increased at a lower rate.
- Analysis by Tony Wood of the Grattan Institute released in March 2015 addressing the anti-privatisation campaign in New South Wales noted the benefits of privatisation in terms of electricity prices to consumers.[7] A detailed comparison between government and private ownership, published in the Grattan Institute's 2012 report found that government-owned companies had more physical infrastructure per customer and spent more on capital investment than did privately owned companies.[8]

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4 Ernst and Young Australia, *Network Pricing Trends, Queensland Perspective*, January, 2015.

5 Australian Industry Group, *AI Group Statement*, January 2015

6 UnitingCare Australia, *Network tariffs applicable to households in Australia: empirical evidence*, Report prepared for UnitingCare Australia by Carbon and Energy Markets, February 2015.

7 Wood, T., NSW power privatisation: *Stop the Sell Off claims put to the test*, The Conversation, 10 March 2015.

8 Wood, T., *Putting the customer back in front: How to make electricity cheaper*, Grattan Institute, December, 2012.

Process for privatisation

1.21 The committee has recommended that any privatisation be based upon rigorous analysis of all costs and be preceded by public consultation. This is precisely what governments ordinarily do as part of considering any option for privatisation. The Commonwealth for example conducts scoping studies, as a means of identifying the most effective approach to deliver a service. Such exercises do not proceed from a bias towards privatisation, rather they are exercises aimed at identifying the best delivery method for a service to the community. A scoping study may for instance recommend better regulation, greater competition, or restructuring of government delivery mechanisms.

1.22 A scoping study is traditionally run by department officials and informed by independent advice from business advisers and legal advisers who have the expertise to assess the relevant service and market in fine detail. This work is done at arms length from Ministers and at arms length from those who currently have vested interests in the market.

1.23 These studies usually involve extensive consultation, including with consumer groups, current providers and potential future providers (including institutional investors). There is nothing new or profound in what the committee majority is recommending.

Arguments against the Asset Recycling Initiative

1.24 Some of the criticisms of the Asset Recycling Initiative are not particularly convincing. Plainly the measure is aimed at encouraging future investment in new infrastructure, but some critics complain that this does not benefit jurisdictions which have undertaken past privatisations. This criticism is not contending that the initiative is innately undesirable, but that it isn't as available as widely as possible. The complaint however shows poor understanding of sound public policy principles. It is normal for any incentive scheme to operate prospectively, where the policy intention is to encourage activity which might not otherwise occur.

1.25 Other critics worry that a 'first come first served' model might disadvantage late comers. Again this is a criticism that a desirable scheme it isn't as available as widely as possible. As we live in a world of finite resources, it is not possible to have an open-ended scheme. Given that the Government has made very clear up front how decisions would be taken, all states and territories begin with the same opportunity to put forward their best cases early.

1.26 The criticism that 15 per cent is not as much as some would like, is another concession that the scheme is intrinsically a desirable one. As the figure was negotiated between the Commonwealth and the states and territories, this figure strikes the right balance to provide a sufficient incentive to unleash locked-up capital.

1.27 Some of the criticism is entirely speculative and counter-intuitive. The majority assert that “there is a distinct risk that states and territories will take shortcuts to avoid thorough and transparent analysis.” In fact, in a competitive scheme, states and territories will be under pressure to present the most convincing analysis. Moreover public interest in privatisations will compel governments to be transparent. Governments are always conscious that if they fail to be sufficiently transparent, they can be held accountable through the democratic process.

1.28 Several participants to the inquiry highlighted the benefits that asset recycling can provide governments. For example, the Australian Logistics Council stated that one of the benefits of asset recycling is its capacity to provide governments with constrained balance sheets the ability to unlock capital tied up in mature assets. It also stated that the idea was by no means novel, noting:

> For instance, the Infrastructure Finance Working Group (established by the previous government in 2011 to provide advice to Infrastructure Australia on infrastructure finance policy) recommended State and Territory governments conduct strategic reviews of ‘brownfield assets’ to: identify and monetise suitable candidates so as to allow the freed up capital and [allow for] avoided debt repayments to be recycled/invested into infrastructure projects.
>
> …the budgets of most Australian governments are likely to be in deficit for the foreseeable future, and likely to remain so, with growing demand for recurrent spending on health, education, NDIS etc. It is therefore necessary to identify alternative funding sources for the roads and infrastructure hitherto regarded as public goods funded from consolidated revenue.[9]

1.29 Finally, the quotation and paraphrasing of the discussion in the Productivity Commission inquiry into Public Infrastructure on asset recycling in the majority report (paragraph 2.68), while noting the Commission’s concerns about risks, omitted to include the Commission’s concluding paragraph which noted:

> [T]he Initiative does not obviate the need for good governance and transparent and sound analysis of privatisation and procurement decisions. Only under these constraints can the additional risks of the initiative be managed in a way that preserves the interests of the broader community.[10]

1.30 As noted above, Government accepts that rigorous analysis of costs and benefits as well as sound decision making processes are necessary to protect the interests of the wider community.

9 Australian Logistics Council, *Submission 12*, p. 4.

10 Productivity Commission, *Public Infrastructure*, Inquiry report, No. 71, May 2014, p. 264.

Comments on recommendations

1.31 **Response to recommendation 1.** This recommendation calling for good processes prior to privatisation decisions, including a full assessment of the costs of projects as well as extensive consultation, is consistent with the Government's proposed policy that the full costs of any privatisation and investment projects as well as an assessment of the benefits should be undertaken, before decisions are made to proceed. It is noted, however, that primary responsibility for this lies with State and Territory Governments.

1.32 **Response to recommendation 2.** The introduction of appropriate regulatory arrangements and safeguards against anti-competitive behaviour are important considerations for governments undertaking privatisation. These are, however, matters for the responsible State and Territory Governments.

1.33 **Response to recommendation 3.** For the reasons outlined in the preceding discussion, this recommendation is not supported.

Senator Sean Edwards
Deputy Chair

Senator Matthew Canavan
Committee Member