



COMMONWEALTH OF AUSTRALIA

Official Committee Hansard

SENATE

ECONOMICS LEGISLATION COMMITTEE

ESTIMATES

(Budget Estimates)

WEDNESDAY, 2 JUNE 2010

CANBERRA

BY AUTHORITY OF THE SENATE

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**SENATE ECONOMICS
LEGISLATION COMMITTEE
Wednesday, 2 June 2010**

Members: Senator Hurley (*Chair*), Senator Eggleston (*Deputy Chair*), Senators Bushby, Cameron, Pratt and Xenophon

Participating members: Senators Abetz, Adams, Back, Barnett, Bernardi, Bilyk, Birmingham, Mark Bishop, Boswell, Boyce, Brandis, Bob Brown, Carol Brown, Bushby, Cash, Colbeck, Jacinta Collins, Coonan, Cormann, Crossin, Farrell, Feeney, Ferguson, Fielding, Fierravanti-Wells, Fifield, Fisher, Forshaw, Furner, Hanson-Young, Heffernan, Humphries, Hutchins, Johnston, Joyce, Kroger, Ludlam, Lundy, Ian Macdonald, McEwen, McGauran, McLucas, Marshall, Mason, Milne, Minchin, Moore, Nash, O'Brien, Parry, Payne, Polley, Ronaldson, Ryan, Scullion, Siewert, Sterle, Troeth, Trood, Williams and Wortley

Senators in attendance: Senators Abetz, Bernardi, Boswell, Brandis, Bob Brown, Bushby, Cameron, Colbeck, Eggleston, Heffernan, Hurley, Joyce, Ian Macdonald, McGauran, Milne, Pratt, Sterle and Xenophon

Committee met at 9.00 am

DEPARTMENT OF THE TREASURY

Consideration resumed from 1 June 2010

In Attendance

Senator Sherry, Assistant Treasurer

Outcome 1—Sound Macroeconomic Environment

Output Group 1.1 Macroeconomic Group

Dr David Gruen, Executive Director
Mr Tony McDonald, General Manager, Macroeconomic Policy Division
Dr Steve Morling, General Manager, Domestic Economy Division
Mr Adam McKissack, Principal Adviser, Forecasting, Domestic Economy Division
Mr Paul Flanagan, General Manager, International Finance Division
Mr Mike Kooymans, Senior Adviser, International Finance Division
Mr Bill Brummitt, General Manager, International and G20 Division
Mr Robert Ewing, General Manager, Macroeconomic Modelling Division
Mr Liangyue Cao, Senior Adviser, Macroeconomic Modelling Division

Outcome 2—Effective Government Spending Arrangements

Output Group 2.1 Fiscal Group

Mr Nigel Ray, Executive Director
Ms Peta Furnell, General Manager, Social Policy Division
Mr Peter Robinson, Principal Adviser, Social Policy Division
Mr Chris Foster, Principal Adviser, Social Policy Division
Mr Damien White, Manager, Social Policy Division

Mr Steve French, General Manager, Industry, Environment and Defence Division
Mr Russ Campbell, Principal Adviser, Industry, Environment and Defence Division
Ms Natalie Horvat, Manager, Industry, Environment and Defence Division
Ms Jan Harris, General Manager, Budget Policy Division
Ms Luise McCulloch, Principal Adviser, Budget Policy Division
Mr Jason Allford, Principal Adviser, Budget Policy Division
Ms Sue Vroombout, General Manager, Commonwealth-State Relations Division

Outcome 3—Effective taxation and retirement income arrangements

Output Group 3.1 Revenue Group

Mr David Parker, Executive Director
Mr Mike Rawstron, General Manager, International Tax and Treaties Division
Mr William Potts, Manager, International Tax and Treaties Division
Mr Greg Wood, Manager, International Tax and Treaties Division
Ms Brenda Berkeley, Secretary, Board of Taxation and General Manager, Indirect Tax Division
Ms Maryanne Mrakovcic, General Manager, Tax Analysis Division
Mr Phil Gallagher, Manager, Tax Analysis Division
Mr Colin Brown, Manager, Tax Analysis Division
Mr John Clark, Manager, Tax Analysis Division
Mr Anthony King, Tax Analysis Division
Mr Marty Robinson, Manager, Tax Analysis Division
Mr Paul McCullough, General Manager, Business Tax Division
Mr Michael Willcock, General Manager, Personal and Retirement Income Division
Mr Tony Coles, Manager, Personal and Retirement Income Division
Mr Trevor Thomas, Principal Adviser, Personal and Retirement Income Division
Mr Nigel Murray, Manager, Personal and Retirement Income Division
Ms Christine Barron, General Manager, Tax System Division
Mr Jason McDonald, Principal Adviser, Tax System Division
Ms Mary Balzary, Principal Communications Adviser, Tax System Division
Mr Brant Pridmore, Manager, Tax System Division

Outcome 4—Well Functioning Markets

Output Group 4.1 Markets Group

Mr Jim Murphy, Executive Director
Mr Richard Murray, Executive Director, Policy Coordination and Governance
Mr Geoff Miller, General Manager, Corporations and Financial Services Division
Ms Vicki Wilkinson, Principal Adviser, Corporations and Financial Services Division
Mr Mark Sewell, Manager, Corporations and Financial Services Division
Mr Daniel McAuliffe, Acting Manager, Corporations and Financial Services Division
Ms Marian Kljakovic, Manager, Corporations and Financial Services Division
Ms Alix Gallo, Manager, Corporations and Financial Services Division
Dr Richard Sandlant, Manager, Financial Services Taskforce
Ms Lorraine Allen, Senior Adviser, Australian Financial Centre Forum
Mr Patrick Colmer, General Manager, Foreign Investment and Trade Policy Division
Mr John Lonsdale, General Manager, Financial System Division

Ms Jacky Rowbotham, Manager, Financial System Division
Mr Justin Douglas, Manager, Financial System Division
Mr Roger Brake, Manager, Financial System Division
Dr Steven Kennedy, General Manager, Infrastructure, Competition and Consumer Division
Mr Brad Archer, Principal Adviser, Infrastructure, Infrastructure, Competition and Consumer Division
Mr Bruce Paine, Principal Adviser, Competition Infrastructure, Competition and Consumer Division
Mr Andrew Deitz, Manager, Infrastructure, Competition and Consumer Division
Mr Paul McBride, Principal Adviser, Cities and Housing, Infrastructure, Competition and Consumer Division
Mr Simon Writer, Manager, Infrastructure, Competition and Consumer Division
Mr Paul Madden, Program Director, Standard Business Reporting Management Group
Mr Greg Divall, Program Manager, Standard Business Reporting Management Group
Mr Peter Martin, General Manager, Australian Government Actuary

Australian Bureau of Statistics

Mr Brian Pink, Australian Statistician
Mr Trevor Sutton, Deputy Australian Statistician, Social Statistics Group
Ms Gillian Nicoll, Assistant Statistician, Office of the Statistician
Mr Paul Lowe, Assistant Statistician, Population Census Branch
Mr Michael Belcher, Chief Financial Officer
Mr Denis Farrell, Deputy Australian Statistician, Population, Labour, Industry and Environment Statistics Group
Mr Ian Ewing, Deputy Australian Statistician, Macroeconomics and Integration Division
Ms Sue Phillips, Acting Assistant Statistician, Corporate Services Division
Mr Peter Harper, Chief Operating Officer
Mr Vince Lazzaro, Assistant Statistician, Human Resources Branch
Mr Garth Bode, First Assistant Statistician, Social Statistics Group

Australian Competition and Consumer Commission

Mr Graeme Samuel AO, Chairman
Mr Brian Cassidy, Chief Executive Officer
Mr Marcus Bezzi, Executive General Manager, Enforcement and Compliance Division
Mr Tim Grimwade, Executive General Manager, Mergers and Acquisitions Group
Mr Mark Pearson, Executive General Manager, Regulatory Affairs Division
Ms Jo Schumann, Executive General Manager, Corporate Division
Ms Michelle Groves, Chief Executive Officer, Australian Energy Regulator
Mr Scott Gregson, Group General Manager, Enforcement Operations
Mr Nigel Ridgway, Group General Manager, Compliance, Research, Outreach and Product Safety
Mr Adrian Brocklehurst, Chief Finance Officer
Dr Richard Chadwick, General Manager, Adjudication Branch
Mr Sebastian Roberts, General Manager, Water Branch
Mr Sean Riordan, General Manager, NBN Engagement and Industry Compliance Branch

Australian Office of Financial Management

Mr Neil Hyden, Chief Executive Officer
Mr Michael Bath, Director, Financial Risk
Mr Gerald Dodgson, Head of Treasury Services
Mr Andrew Johnson, Head of Compliance and Reporting
Mr Pat Raccosta, Chief Finance Officer

Australian Prudential Regulation Authority

Dr John Laker, Chairman
Mr John Trowbridge, Member
Mr Keith Chapman, Executive General Manager
Mr Senthamangalam Venkatramani, General Manager

Australian Taxation Office

Mr Michael D'Ascenzo, Commissioner of Taxation
Mr David Butler, Second Commissioner
Mr Bruce Quigley, Second Commissioner
Ms Jennie Granger, Second Commissioner
Mr Mark Konza, Deputy Commissioner, Small and Medium Enterprises
Ms Raelene Vivian, Chief Operating Officer
Mr Neil Olesen, Deputy Commissioner, Superannuation
Mr Robert Ravanello, Chief Finance Officer

Australian Securities and Investment Commission

Mr Tony D'Aloisio, Chairman
Ms Belinda Gibson, Deputy Commissioner
Mr Michael Dwyer, Commissioner
Mr Justin Owen, Manager, Government Relations
Mr Matthew Abbott, Senior Executive Leader, Corporate Affairs

Productivity Commission

Mr Gary Bank AO, Chairman
Dr Michael Kirby, Acting Head of Office
Ms Lisa Gropp, Principal Adviser, Research
Mr Terry O'Brien, First Assistant Commissioner

CHAIR (Senator Hurley)—I declare open this public hearing of the Senate Economics Legislation Committee. The Senate has referred to the committee the particulars of proposed expenditure for 2010-11 and related documents for the portfolios of Innovation, Industry, Science and Research; Resources, Energy and Tourism; and Treasury. The committee must report to the Senate on 22 June 2010 and has set 30 July 2010 as the date by which answers to questions on notice are to be returned. Under standing order 26, the committee must take all evidence in public session. This includes answers to questions on notice. Officers and senators are familiar with the rules of the Senate governing estimates hearings. If you need assistance, the secretariat has copies of the rules. I particularly draw the attention of witnesses to an order of the Senate of 13 May 2009 specifying the process by which a claim of public interest immunity should be raised, which I now incorporate in *Hansard*.

The extract read as follows—

Public interest immunity claims

That the Senate—

- (a) notes that ministers and officers have continued to refuse to provide information to Senate committees without properly raising claims of public interest immunity as required by past resolutions of the Senate;
- (b) reaffirms the principles of past resolutions of the Senate by this order, to provide ministers and officers with guidance as to the proper process for raising public interest immunity claims and to consolidate those past resolutions of the Senate;
- (c) orders that the following operate as an order of continuing effect:
 - (1) If:
 - (a) a Senate committee, or a senator in the course of proceedings of a committee, requests information or a document from a Commonwealth department or agency; and
 - (b) an officer of the department or agency to whom the request is directed believes that it may not be in the public interest to disclose the information or document to the committee, the officer shall state to the committee the ground on which the officer believes that it may not be in the public interest to disclose the information or document to the committee, and specify the harm to the public interest that could result from the disclosure of the information or document.
 - (2) If, after receiving the officer's statement under paragraph (1), the committee or the senator requests the officer to refer the question of the disclosure of the information or document to a responsible minister, the officer shall refer that question to the minister.
 - (3) If a minister, on a reference by an officer under paragraph (2), concludes that it would not be in the public interest to disclose the information or document to the committee, the minister shall provide to the committee a statement of the ground for that conclusion, specifying the harm to the public interest that could result from the disclosure of the information or document.
 - (4) A minister, in a statement under paragraph (3), shall indicate whether the harm to the public interest that could result from the disclosure of the information or document to the committee could result only from the publication of the information or document by the committee, or could result, equally or in part, from the disclosure of the information or document to the committee as in camera evidence.
 - (5) If, after considering a statement by a minister provided under paragraph (3), the committee concludes that the statement does not sufficiently justify the withholding of the information or document from the committee, the committee shall report the matter to the Senate.
 - (6) A decision by a committee not to report a matter to the Senate under paragraph (5) does not prevent a senator from raising the matter in the Senate in accordance with other procedures of the Senate.
 - (7) A statement that information or a document is not published, or is confidential, or consists of advice to, or internal deliberations of, government, in the absence of specification of the harm to the public interest that could result from the disclosure of the information or document, is not a statement that meets the requirements of paragraph (1) or (4).
 - (8) If a minister concludes that a statement under paragraph (3) should more appropriately be made by the head of an agency, by reason of the independence of that agency from ministerial direction or control, the minister shall inform the committee of that conclusion and the reason for that conclusion, and shall refer the matter to the head of the agency, who shall then be required to provide a statement in accordance with paragraph (3).

(Extract, Senate Standing Orders, pp 124-125)

[9.02 am]

CHAIR—The committee will begin today's proceedings by continuing its consideration of the Treasury Macroeconomic Group and will then follow the order as set out in the circulated program. I again welcome the Assistant Treasurer, Senator Sherry; and officers of the department. Dr Gruen or Minister, would you like to make an opening statement?

Senator Sherry—I do not wish to make an opening statement.

Dr Gruen—Nor do I.

CHAIR—Thank you.

Senator JOYCE—The projected surplus in 2012-13 falls in a projection period as opposed to an estimates period of budget. Do you agree with that statement?

Dr Gruen—The macroeconomic forecasts are in the years 2009-10, 2010-11 and 2011-12, and then 2012-13 is the first projection year. That is correct.

Senator JOYCE—Can you, for the purposes of *Hansard*, tell us briefly the difference between a projection and an estimate.

Dr Gruen—And a forecast, you mean.

Senator JOYCE—And a forecast—sorry.

Dr Gruen—I can. As you would be aware, macroeconomic forecasting is a difficult business and it is increasingly difficult the further out you look. We, along with most other organisations, make the judgment that beyond a certain point we cannot do any better than forecasting that the economy will grow at trend, so our standard assumption is that at the current point, beyond 2011-12, we simply assume that the economy will grow at trend. We do make some exceptions to that general rule. For instance, as you would be aware, in last year's budget, because at that time we thought the economy was going to be a long way below its potential at the end of the forecast period, we changed our medium-term projection assumptions and assumed that the economy would be growing above trend in the projection years, at least for several of them. However, given that the outcome has turned out so much more favourably than we had expected, we have reverted to our standard assumption that growth would be at trend in the projection years. This is always a matter of judgment and we apply a slightly different assumption for the terms of trade, which I am happy to go into if you want me to.

Senator JOYCE—You would agree that the government has lauded the billion dollar surplus in 2012-13. It is one of the—

Dr Gruen—I am not going to comment on that.

Senator JOYCE—Do you agree that the government has stated that there will be a surplus in 2012-13?

Dr Gruen—The forecasts are that there will be a small surplus in 2012-13, a surplus in the order of 0.1 per cent of GDP, I think.

Senator JOYCE—Point one per cent of GDP—so, a billion dollar surplus. That is about a \$400 billion gross budget. So 0.1 per cent is a very small fraction. Can you tell me any cost

you have had that has come within 0.1 per cent of its prediction—when you take things out to the forecast level? Have you had one forecast ever that has not varied by more than 0.1 per cent?

Dr Gruen—I suspect you do not want me to take that question on notice. But I cannot give you an iron-clad guarantee one way or another. But I am certainly willing to say that 0.1 per cent of GDP is a small surplus—there is not question about that. It is a small number.

Senator JOYCE—In the past, I have offered a bet. I have said, ‘If you can do 0.1 per cent or better, I will give you \$1,000; and if it is 0.1 per cent or worse, will you give me \$1,000?’

Dr Gruen—Senator, I am not in the business of engaging in public bets with—

Senator JOYCE—I am in the business of making money and I think this is a sure thing.

Dr Gruen—I am not in the business of making bets. There are both upside and downside risks to all of our forecasts.

Senator JOYCE—Give me some of the downside ones that are obviously in the news at the moment.

Dr Gruen—Downside risks that are in the news?

Senator JOYCE—Yes.

Dr Gruen—I will give you both upside and downside; I will try and be balanced. On the downside, the fiscal situation in Europe is clearly going to play out over an extended period of time and generate bouts of market volatility. The fiscal situation in Europe is very serious. How that is resolved remains to be seen. So that is, I would think, the largest obvious event going on out there at the moment that is a downside risk. On the upside, we continue to see very strong data coming out of Asia—China, but also other East Asia economies, including India. Despite recent falls in commodity prices, commodity prices remain at very high levels and in fact are consistent with further increases in negotiated contract prices for bulk commodities over the next three months. So I would say that there are significant risks in both directions.

Senator JOYCE—Bulk commodities such as what?

Dr Gruen—The main bulk commodities are obviously iron ore and coal. As to which of those has spot prices above the current contract prices, I think both of them do.

Senator JOYCE—Is there anything on the horizon at the moment that might affect our export of bulk commodities to those Asian markets—any government policy around that the industry has stated might affect their capacity to grow and export? Is there any government policy that you can bring to mind?

Dr Gruen—Certainly the industry has made statements about the resource super profits tax.

Senator JOYCE—If that affected bulk commodities—if they were right—would that affect our surplus?

CHAIR—They are not right.

Senator JOYCE—But, if their statement is right, would that affect our surplus?

Dr Gruen—I do not think that I should be speculating on whether industry statements are right or not.

Senator JOYCE—Even if it affected things to the extent that it changed by 0.1 per cent?

Dr Gruen—Our forecasts for commodity exports and for the terms of trade and for growth were put together in light of the resource super profits tax. So we were well aware of the details of the resource super profits tax when we put our forecasts together. Our forecasts for non-commodity exports I think are pretty similar to those of the Reserve Bank, which also put its latest forecasts together in light of the resource super profits tax. There will be different views about the implications of that policy on exports, but our considered view, which is the same as the Reserve Bank's considered view, is that we are going to see very strong investment in that sector and exports.

Senator JOYCE—Okay. When you modelled it, you modelled it taking into account the resource super profits tax. Now, did that modelling show a reduction, in any way, shape or form, because of this new tax?

Dr Gruen—We do our forecasts both from the bottom up and from the top down, and—

Senator JOYCE—I will put it another way: did you forecast it would be exactly the same if the tax had not been there?

Dr Gruen—I think our forecasts were that it did not make a material difference.

Dr Morling—Senator, if I could reply. The way we do the forecasts which are most relevant to the mining sector and which you are alluding to is on a bottom-up approach, and almost all the projects we include in our forecasts for the following two years are projects that are already under construction. So if the tax were to have any effect either way, positive or negative, it would not really show up in our engineering construction forecast because of the time frame in which we are measuring the progress of these large companies.

Senator JOYCE—That is the main answer I want. So it is like the tax was not there; that is how you forecast the surplus?

Dr Morling—The tax will have no effect on our engineering construction forecast or on our GDP numbers over that time horizon.

Senator JOYCE—That is interesting. What happens if there is a negotiated settlement and they change the upload factor, the bond rate, from 5.75—

Senator Sherry—Senator, that is not an issue for the officials. You referred to a negotiated settlement—

Senator JOYCE—Okay. I will be more direct.

Senator Sherry—No, just let me finish. You referred to a negotiated settlement, which is a direct issue of policy and appropriately comes to me.

Senator JOYCE—Rightio. I will go straight to the point. Do you take into account in your revenue forecast the bond rate of 5.75 per cent that is part of the calculations of the tax that goes into the revenue statement of the budget?

Dr Gruen—Senator, you should not ask us about the revenue forecasts. We are—

Senator JOYCE—In the discussion of the surplus, do you take into account the uplift factor for the bond rate?

Dr Gruen—I guess you could ask the question, if you wanted to, of Fiscal Group about what they take into account in the surplus. But I can answer the question from the perspective of our macroeconomic forecasts. We obviously make a judgement about the implications of the tax as it was announced.

Senator JOYCE—So, if they change the tax, they change the outcome?

Dr Gruen—In principle, it could.

Senator JOYCE—Right. Thank you. The economic forecasts in table 1 of Budget Paper No. 1, on page 1-7 and repeated elsewhere, show a low in the unemployment rate of 4¾ per cent—

Dr Gruen—Yes.

Senator JOYCE—over the next four years. That is despite at least one year of above-trend growth in 2011-12 and roughly trend growth in other years.

Dr Gruen—Yes.

Senator JOYCE—The low point in the unemployment rate in recent years was four per cent, seasonally adjusted, in February-March, and the unemployment rate was at or below 4¾ per cent between July and December. What has changed in the economy that Treasury no longer believes that the recent lows in the unemployment rate can be attained over the next four years?

Dr Gruen—There are a couple of parts to this answer. It has been our longstanding practice at least since 2002 to make an assumption that the full rate of unemployment is five per cent. We have not had any reason to change that assumption over the time. We first made that assumption to my knowledge in the first *Intergenerational report* which was released with the 2002-03 budget. Ever since then we have regarded that as a reasonable number for full employment. Having said that, we make an assumption which is a particular number, namely five per cent, but there is a reasonable band of uncertainty around that number. With the best will in the world, we cannot really tell whether it is five per cent or anywhere in the range, say, from about 4¾ to 5¼ per cent. The full employment rate of unemployment could in principle be outside that range.

So then the question is: how come it was possible for unemployment to fall all the way down to four per cent as it did a few years ago? The answer is that it is always possible for unemployment to fall below its full employment rate. If you have understood how the economy works accurately, then the implication of that falling below the full employment rate ought to be that inflation starts to rise. From 2006 to 2008 what we saw was the underlying rate of inflation rising from around 2½ to around 4½. As I say, there is nothing exact in any of this but the behaviour of inflation as the unemployment rate came down to four per cent was entirely consistent with those unemployment rates being inconsistent with steady inflation.

So it is not that the economy cannot generate lower rates of unemployment; it is just that if you do go below the full employment rate, you will end up with rising inflation. As a

consequence of the rising inflation, interest rates went up and the economy was slowing and then of course the global financial crisis turned up.

Senator JOYCE—Obviously, we are between four per cent and $4\frac{3}{4}$ per cent. With a bit more than an 11 million workforce, that is about 88,000 people. Saying that four per cent is a more reasonable expression, what moves would we need to take in a policy direction to get these 88,000 people back into the workforce?

Dr Gruen—The important thing to note is that the four per cent unemployment rate was not sustainable in the sense that it was associated with rising inflation, and the Reserve Bank saw it necessary at that time to raise interest rates. It does not help anyone to have the unemployment rate at a level that is generating rising inflation and it is not sustainable, and that was the situation as it was.

Senator JOYCE—So, if you raise employment, you raise inflation, so you have to raise interest rates.

Dr Gruen—What we are talking about here is what is commonly known as the NAIRU, which is the rate of unemployment you can sustain without putting pressure on inflation. As I said, there can be some discussion about what that level is, and in Treasury we have assumed for several years now that that level is five per cent, although we do not claim any particular level of precision about that estimate. It is five per cent with a margin of error around it. For the sake of the conversation, if it is the case that the NAIRU is five per cent, you cannot sustain an unemployment rate of four per cent because, when that rate comes down to four per cent, inflation starts to rise and you end up in a situation which is inconsistent with the Reserve Bank's mandate, and so they act.

Senator JOYCE—What do you believe the NAIRU is at the moment?

Dr Gruen—Around—as I said, I do not want to make—

Senator JOYCE—Around five per cent.

Dr Gruen—Around five per cent, with some significant margin of error.

Senator JOYCE—So, if you had a stimulatory process that was excessive in the increase in employment, you would have to raise interest rates to cool the economy down?

Dr Gruen—If you ended up with any policy which drove the unemployment rate below the NAIRU then, as a consequence of that, other actions would need to be taken—whether by the Reserve Bank or by someone else—to slow the economy down.

Senator JOYCE—But, as you approached the NAIRU, you would start raising interest rates, wouldn't you?

Dr Gruen—It would depend on a whole lot of things. One makes judgements not only about the NAIRU but about prospects in the future and about the level of the currency—there are a whole lot of things that one would take into account.

Senator JOYCE—What policies would reduce the sustainable level of unemployment?

Dr Gruen—What policies would reduce the NAIRU?

Senator JOYCE—Yes.

Dr Gruen—I think it is fair to say that the changes that Australia has made over the past couple of decades to move away from centralised wage bargaining to more enterprise based bargaining have seen some decline in the NAIRU. Wage negotiations that are conducted on an enterprise basis usually lead to a situation where the NAIRU is lower. But this is tricky because it is also true that the accord period in the 1980s was a period of centralised wage fixing, which, most commentators agree, was also associated with considerable wage moderation. This is a tricky area and it is hard to be categorical.

Senator JOYCE—So, the more flexibility there is in the labour market, the more capacity there is for employment?

Dr Gruen—It is not that simple, as a comparison with the US at the moment would make clear. The US has a very flexible labour market and unemployment near 10 per cent. I am not necessarily disagreeing with you; I am just saying that this is not an area where we can make categorical statements. But I think most economists would agree that moving the bargaining unit so that enterprises bargain with their workers to determine outcomes creates an environment in which the NAIRU is lower than it would be in an environment in which those decisions were made at a simple level.

Senator JOYCE—Thank you for that. What are your thoughts on the statements about Australia in the OECD's *Economic policy reforms: going for growth 2010*, released in March, where they said:

A 2006 reform fostered individualisation of labour relations and an independent body was created to set the federal minimum wage, taking into account its employment impact. These measures were partly reversed in 2008 through a reinforcement of the role of awards, raising the risk of increases in minimum labour costs ...

Are the reversals that the OECD talks about a risk to the performance of Australia's labour market in future economic downturns?

Dr Gruen—Sorry, can you read the statement again?

Senator JOYCE—In summary, what are your thoughts on the OECD's 'going for growth study' on Australia released in March and are the reversals that the OECD talks about a risk to the performance of Australia's labour market in future economic downturns? If you want me to go through the quote, it was, and it is talking about Australia, obviously:

A 2006 reform fostered individualisation of labour relations and an independent body was created to set the federal minimum wage—

Senator CAMERON—Back to Work Choices. That is where we are with you lot.

Senator JOYCE—It continues:

... taking into account its employment impact. These measures were partly reversed—

Senator CAMERON—We know where you lot are going—Work Choices.

Senator JOYCE—It continues:

... in 2008 through a reinforcement of the role of awards, raising the risk of increases in minimum labour costs ...

CHAIR—Order! Senator Joyce, can you just stop for a moment?

Senator Bernardi interjecting—

CHAIR—Senator Bernardi and Senator Cameron, can you please allow Dr Gruen to hear the question? Senator Joyce, please continue.

Senator CAMERON—We know what you are trying to do.

Senator Sherry—Sorry, Chair, I am afraid will have to ask Senator Joyce to repeat the question, because of the very unhelpful interjections from a number of senators.

Senator JOYCE—I will repeat it again. That is a good statement, Minister; we will try and keep it simple. Dr Gruen, I will have another crack at it. What are your thoughts on the OECD's 'growing for growth' study on Australia released in March, where they said:

A 2006 reform fostered individualisation of labour relations—that was obviously, in Australia—and an independent body was created to set the federal minimum wage, taking into account its employment impact. These measures were partly reversed—in Australia—in 2008 through a reinforcement of the role of awards, raising the risk of increases in minimum labour costs ...

Are the reversals that the OECD talks about a risk to the performance of Australia's labour market in future economic downturns?

Dr Gruen—The OECD is talking about the setting of minimum wages, as I understand it. The claim that they are making is that that is raising the risk of minimum wages growing more rapidly or ending up higher than they were under the previous institutional arrangements. I guess my answer to that would be simply that we have the track record of the institution—I forget what the name it is—that was run by Ian Harper. Was that called Fair Work Australia?

Senator Sherry—The Fair Pay Commission.

Dr Gruen—Thank you, Senator. We have a track from the Fair Pay Commission. We do not yet have a track record from the new body that has been set up. So I guess my main answer to this is that it is too early to be making statements about risks. It is certainly the case that fair pay commissions need to take into account both the pay for the low paid and also the implications of changes in the minimum wage for employment prospects. I think that is definitely the case—that is what these bodies need to take into account—but I am not really in a position to comment on whether the new institutional arrangements for low-paid workers will generate risks for higher outcomes than under the alternative arrangements. I just think it is too early to say.

Senator JOYCE—Thank you, Dr Gruen, but you were in 2006—

Dr Gruen—I was.

Senator JOYCE—I am going to quote back to you now. Dr Gruen—you are a person I read a lot about—in a speech in 2006 stated:

Australia's institutional settings—which include a market-determined exchange rate, medium-term monetary and fiscal policy frameworks as well as a flexible labour market—have given the economy the flexibility needed to deal with different economic shocks and helped to largely avoid problems that arose in previous terms of trade booms.

Do you stand by those comments?

Dr Gruen—Yes—I wrote them.

Senator JOYCE—Taking into account the benefits of a flexible labour market, its capacity to keep Australians employed, the uncertainties that are currently before us, the problems that the government are creating for themselves in their latest foray into nationalising the mining industry, do you believe that it would be prudent for us to have the capacity to move those people from one section of employment to another section of employment with the flexibility that actually keeps them in jobs?

Dr Gruen—Obviously I am not going to comment on parts of that question.

Senator Sherry—It was rhetoric and statement. Most of it was not a question.

Dr Gruen—The statement that you read out, which I wrote in 2006, talked about the benefits of a range of institutional features of the Australian economy, including a floating exchange rate, medium term frameworks for monetary and fiscal policy and a flexible labour market. I do think that those features, including the last one, are important features to enhance the capacity of the economy to respond to shocks. I would note that, in the most recent significant slowdown that was associated with the global financial crisis, we have seen a significant slowing in wage costs as measured by the wage cost index, especially in the private sector. That leads me to think that there is significant flexibility in the Australian labour market. But I certainly agree with the statement which says that there are significant benefits in having wage flexibility when responding to shocks.

Senator IAN MACDONALD—I thank Senator Abetz and Senator Eggleston for allowing me two minutes to ask just one question. Was any modelling done that looked at the impact of the mining tax on regional and remote businesses, the north-west mineral province, Northern Australia or anything? I am really looking at what impact the mining tax might have on communities like Cloncurry, Mount Isa, Mackay and towns in the Bowen Basin coalfields area—not so much the mining tax itself but the impact it might have on those areas. Was that sort of modelling done?

Dr Gruen—I believe a question very similar to that one was asked of Dr Henry last week. If my memory is correct, his answer was that, as far as he was aware, we had not done any modelling of the regional impact. To the extent that modelling was done, it was not released.

Senator IAN MACDONALD—I can read what Dr Henry said. He said that he was not aware if we—I assume ‘we’ means you people—

Dr Gruen—Treasury.

Senator IAN MACDONALD—‘We’ meaning you people at the table.

Dr Gruen—That is right.

Senator IAN MACDONALD—Surely someone here will know whether or not you have done that modelling.

Dr Gruen—I was just continuing.

Senator IAN MACDONALD—I am sorry.

Dr Gruen—Part of the KPMG Econtech modelling is an economy-wide model. An economy-wide model will, as part of the modelling, generate results for the disaggregated

regions that are in that model. I am not fully on top of the detail of how much disaggregation is in the Econtech model, though we may well have people here who know more about that than I do. I am not aware of whether that regional dimension has been published. I do not think it has. I do not think the results from the regional analysis have been published. We could take it on notice, if you would like.

Senator IAN MACDONALD—Dr Gruen, you made the invitation, which I gratefully accept, that there may be other people in the room who have the information. I cannot believe that not one of the six top people from Treasury knows whether or not regional modelling was done. You have indicated in words that I do not quite understand that, because it is an economy-wide model, it will pick up the regional impacts.

Dr Gruen—Yes.

Senator IAN MACDONALD—So does that mean, yes, there is information? I am not at this stage asking whether I can see it. I am asking: is there work done that would indicate the impact on the regions?

Senator Sherry—We are just checking for you, Senator, to see if there is anything already available.

Mr Ewing—I should begin by clarifying that my area is not responsible for the MM900 model from Econtech that was used and so I am not the world's greatest expert on it; however, I can tell you that—

Senator IAN MACDONALD—You are probably better than most of us on this side of the table.

Mr Ewing—To the best of my knowledge, it does not have the regional dimension that you are asking about, in that it does not have substate regions within the model. Its primary focus is on national results and industry results. Those would give you some insight into the impacts on regions, but you have to do that outside of the model rather than having a nice model that tells you that Mount Isa does this or that.

Senator IAN MACDONALD—I am not talking about Mount Isa so much as the impact on all of non-big-city Australia. It is really remote Australia where most of the mines are.

Mr Ewing—My understanding is that the modelling that was done for Treasury by KPMG Econtech does not include that dimension.

Senator IAN MACDONALD—So you disagree with what Dr Gruen said—that the economy-wide model will generate results for disaggregated regions?

Mr Ewing—I never like to disagree with Dr Gruen. There are many disaggregated results that would inform your understanding of the different regions. It is simply that the model does not do the work for you. You have to take the results of the model and apply them yourself.

Senator IAN MACDONALD—Okay. Has anyone in Treasury taken the results and applied them themselves?

Mr Ewing—My area has not.

Senator IAN MACDONALD—Perhaps I can come back to Dr Gruen.

Dr Gruen—Let me just clear up the apparent suggestion that Robert and I have some fundamental disagreement about the KPMG Econtech model. I have a broad overview of that model and Mr Ewing has a more detailed knowledge than I do. So I defer to him when it comes to what level of disaggregation—

Senator IAN MACDONALD—Mutual admiration!

Dr Gruen—Absolutely.

Senator IAN MACDONALD—Forget that.

Dr Gruen—But you brought it up, Senator.

Senator IAN MACDONALD—I am not here to play a game. I just want to know whether those economy-wide models do generate results for a disaggregated region. I am getting half answers from both you and Mr Ewing. All I want to know is what the impact is on that part of Australia.

Dr Gruen—I do understand. We are not in a position to give you definitive answers because this modelling was commissioned by the Treasury from KPMG Econtech. We in the macro-economic group did not commission the modelling. So you really should talk to the people who did commission the modelling if you want more detailed information about what is in it.

Senator JOYCE—How about a sectoral analysis on agriculture? Did you do that?

Dr Gruen—As I said, the macro-economic group did not do any sectoral analysis of the effects of the RSPT.

Senator IAN MACDONALD—I understand, from very strange circumstances, that someone in Treasury either has done that work or is aware of the answers that I am trying to get. I understand someone in Treasury knows the answer to my questions, whether it is you guys or someone else. On the assumption that it is there, is that the sort of thing that you would make public?

Dr Gruen—To be told that there is someone in Treasury who knows something and then be asked what am I going to do about it—

Senator Sherry—We have heard that line before.

Senator IAN MACDONALD—I am really not here to play a game. There is information that I want to get about the impact, not so much on the mining industry, but on all of those communities, towns and regions that are hugely impacted by the wealth or otherwise of the mining industry. I understand modelling has been done. You are saying you do not know and I accept that. Rather than waste the time of everyone here, because I am obviously not going to get much more this group at the table—or am I? Can you confirm that?

Dr Gruen—I do not have any more information.

Senator IAN MACDONALD—When you said I should ask the right people, who are the right people?

Dr Gruen—Revenue Group commissioned the modelling.

Senator IAN MACDONALD—Minister, could you take my questions on notice for the Revenue Group?

Senator Sherry—Yes, I will.

Senator IAN MACDONALD—I would be very grateful, bearing in mind that I understand the information is available. Whether or not you can release it to me is one thing, but denying that it is there or otherwise is of course quite a separate thing. I appreciate your advice, Minister, that you will take it on notice.

Senator ABETZ—Yesterday we did not quite get to the answer to this question: how much company tax and royalties did mining companies pay last year?

Dr Gruen—That is a question for Revenue Group.

Senator ABETZ—Do we have that available?

Senator Sherry—No, we finished them yesterday.

Senator ABETZ—It is just not known by Dr Gruen and others at the table?

Dr Gruen—I certainly do not know the dollar amount, but I would imagine it is available.

Senator ABETZ—Yes, pretty easily, so if somebody could look that up for us and let us know, say, after morning tea that would be helpful.

Senator Sherry—We are not going to have time imposed on us by you, Senator. I will take it on notice and I will do the best I can.

Senator ABETZ—That is why I said it would be very helpful. I am not imposing anything; I am only asking.

Senator Sherry—I will go back to Revenue Group; we will get someone in Treasury to see if the figure is available. We will get back to you as soon as is practicable.

Dr Gruen—Senator, can I get you to define as precisely as possible what the question is?

Senator ABETZ—How much company tax and royalties did the mining sector pay last year—

Dr Gruen—Last financial year?

Senator ABETZ—Last financial year.

Dr Gruen—In '08-09?

Senator ABETZ—That would be the last financial year, yes. In relation to the pie charts that were in Mr Swan's economic update from last month, in May, I had some discussion with Dr Henry about those charts and I understand the information for those charts went to the Treasurer's office but the Treasurer's office put the pie charts together. Is that correct?

Dr Gruen—Again, Senator, this is an issue for Revenue Group.

Senator Sherry—Certainly Senator Joyce and Revenue Group had a considerable exchange about this yesterday. I do not know whether you are aware of that.

Senator ABETZ—Yes, and I am just trying to follow up on those matters which were not fully nailed down.

Dr Gruen—I am sorry; it is not something that I can comment on, I am afraid.

Senator ABETZ—That is fine. If Senator Joyce has a few more questions I might let him go at this stage and I will come back to some other matters that have been raised with me.

CHAIR—I have other senators on the list—Senator Eggleston and Senator Milne.

Senator EGGLESTON—One of the consequences of the proposed resources super profits tax is that there is an increase in the total tax from the resource sector, and budget projections show an increased revenue of \$3 billion and \$9 billion in 2012-13 and 2013-14 respectively. Can you explain to the committee the reasoning behind the concept that increasing the total tax take from an industry can lead to an increase in investment and growth?

Dr Gruen—Again, I am not the expert on this; but I can make a general comment. If a tax is more efficiently designed, it can raise more revenue while generating less distortions in the sector. Certainly, that is the point of this tax. The problem with royalties are that they take no account of the profitability of the mine. In principle, a royalties regime can make mines which, in the absence of taxation would be profitable—they can render them not worth proceeding with. So, if you get rid of the royalties or if you rebate the royalties and introduce a tax which is more efficient, in principle and in practice you can generate more revenue as well as reduce the distortions in the industry.

Senator EGGLESTON—On the subject of royalties, the Premier of Western Australia, Colin Barnett, makes the point that constitutionally the states own the minerals, and the royalties are the price that the state sells the minerals to the mining companies for. So that is in fact a business cost to the mining companies. Would you like to comment on that proposition?

Dr Gruen—I need to have enough understanding of the tax to be able to make coherent macroeconomic forecasts, but I am not the Treasury expert in this area. I did not work on the Henry tax review or the AFTS team. You really need to address these questions to the people who are the experts.

Senator EGGLESTON—Nevertheless, it is a fundamental constitutional concept that the states own the minerals.

Senator Sherry—There are two issues you raise. One is the revenue issue. There was an opportunity yesterday to deal with that and, as Dr Gruen said, macro did not design the tax or do the revenue estimates et cetera—that was not their job. Secondly, you raise a constitutional issue, a legal issue. There may be someone else in some other area of Treasury but that again is right outside the parameters of the macro group of Treasury. Thirdly, I think the claims—and I would put it no higher than ‘claim’—about who owns what is a legal issue and not for macro.

Senator EGGLESTON—Thank you, Minister. But I would have thought it was fundamental to the thinking underlying this proposal and I would have thought that most officials within Treasury would be familiar with the underlying issues. They are not proposing to abolish royalties; we are talking about rebating under this.

Senator Sherry—we have well outlined who is responsible for what. What I can say is that the Commonwealth is advised that the RSPT is supported by the Constitution’s taxation

power, as it is a tax on profits made from extracted resources. Resources cease to be the property of the state once they are extracted. The RSPT is levied on the resource profit made by the miner. We believe it is constitutional. The government will implement the RSPT in a way that is consistent with Australia's legal framework, rights and obligations, and we will continue to consult with the states and territories on the issue.

Senator EGGLESTON—You said the royalties cease to be the property of the states once they are extracted. That in a way confirms my point, because at that point the states have sold the minerals to the mining companies. But we will move on from there because I can see that we are not going to get a clear and definitive answer. How confident is Treasury that the changes proposed by the government will both increase the tax taken from the mining industry and lead to an increase in investment and growth?

Dr Gruen—The basis of the statement that they would lead to an increase in investment and growth was the long-term modelling done by KPMG Econtech. For the purposes of the macroeconomic forecasts, which take us, as we discussed earlier, out to 2011-12, those forecasts are built-up from all the things that are going on in the economy. The long-term implications of the RSPT are not really relevant to those forecasts over the next couple of years. I think they are really different things.

Senator EGGLESTON—Could you perhaps explain to the committee why mining companies with international operations will not move investment and jobs to a lower taxing jurisdiction. I think that one of the things we tend to underestimate in Australia is how international the mining industry is. Other countries, like Indonesia and countries in Africa and South America, have minerals. Why shouldn't these companies just move to a lower-taxing jurisdiction if we increase our taxes to the level we are proposing?

Dr Gruen—Again, I think this was handled by Dr Henry last week. The general point is that, to the extent that it is profitable to extract the minerals in the ground or off the coast of Australia, the design of the RSPT is such that it remains profitable. It is clearly the case with extremely profitable mines that less of the profits will accrue to miners but it is still the case that the design of the profits tax does not change the point at which the mine becomes profitable. The rate of return on capital invested should not change under the design of the RSPT. As I said, this is not really my area of expertise. I am tasked with putting together the macroeconomic forecasts, taking into account the resource super profits tax—and that is what we have done. Our judgements about the implications of that tax over the next couple of years are pretty close to the judgments made independently by the Reserve Bank when they put their forecasts together in the immediate aftermath of the announcement of the tax. We are forecasting a continuation of very high investment in mining over the next few years on the grounds that it continues to be highly profitable.

Senator EGGLESTON—Thank you. Nevertheless, a number of mining companies have cancelled plans for expansion in Australia and I think that cannot be ignored as an indicator of what might happen.

Dr Gruen—I am not sure that that is so clear. Much of the mining investment that is in our forecasts is already under construction, so precisely what mining companies are going to do with future plans is, I guess, something that is part of the process of consulting with the

government. The mining companies are trying to maximise returns to their shareholders by behaving in a way that does that.

Senator EGGLESTON—No-one can predict the future, and I agree that one cannot say with certainty that various projects will not go ahead, but there are indications that that may be what happens. For example, I went to an Indonesia-Australia Business Council breakfast at UWA last week at which someone spoke about the mining industry in Indonesia. They said that the view in Jakarta now was that Australia had a higher sovereign risk profile than Indonesia as a result of the proposed introduction of this tax.

Senator Sherry—Senator, reflecting on past episodes in history and issues that have affected the resources sector, I can recall three or four. Firstly, with the proposed introduction of the tax regime on offshore oil and gas the claims at the time were that the industry would cease to exist—no investment; that would be it. There was doom and gloom—the sky would fall in; the world would come to an end. That did not happen. We heard a similar set of claims when the Mabo decision was handed down. That did not happen.

Senator JOYCE—That did kind of affect the mining industry, to tell you the truth.

Senator Sherry—We heard a similar set of claims when the gold sector was included in tax. That did not happen. The fourth set of claims that I can recall from the mining sector was that if Work Choices was repealed it would be the end of the world as well. That has not happened. We have seen an extraordinary range of doom and gloom claims over the last 20 years, and they have not happened.

Senator EGGLESTON—We will have to wait and see what the outcome of this is, because—

Senator Sherry—History is with us. On four occasions the claims that were made at the time by some in the mining sector did not happen.

Senator JOYCE—But they do not have to close down. They just have to slow down and your surplus is gone.

Senator ABETZ—That is right.

Senator EGGLESTON—That is right. We will have to wait and see, I think. I take your point; nevertheless, this does change the feeling about the safeness of Australia as a place for very large investment in mining projects. It changes perception about the profitability of those investments.

Senator Abetz interjecting—

Senator Sherry—Senator Abetz interjected with: ‘The GST.’ We made a lot of claims about the GST—

Senator Abetz interjecting—

Senator Sherry—I do not seem to recall that we made a claim that sovereign risk would be increased as a consequence of the GST. It was not true and it would not have happened, as it will not happen in respect of this tax.

Senator ABETZ—If you could have you would have. But sovereign risk does not apply to GST. That is just silly.

Senator EGGLESTON—Exactly. Sovereign risk does apply when mining companies based in London and New York or Zurich are considering—

CHAIR—Senator Eggleston, do you have a question?

Senator EGGLESTON—Yes, I do. Could you explain—

Dr Gruen—I just want to respond to the comment you made. I think it is worth responding to.

Senator EGGLESTON—Please go ahead, Dr Gruen.

Dr Gruen—It has been the case over the past quarter of a century in Australia that governments of both political persuasions have instituted economic reform, and that economic reform has at times led to costs being imposed on existing plant and infrastructure. Let me give you an example. When tariffs are cut the consequence is that existing firms in the traded sector—for example, the car industry—make less profit than they would have if there had not been a tariff change. It has been a widely accepted principle that if governments are not in a position to make any changes to tax rates or tariffs then we simply cannot do economic reform in this country.

Senator EGGLESTON—Thank you, Dr Gruen. In the case of the car industry, of course, taking away the tariffs meant the Australian—

Senator CAMERON—Is there a question?

Senator EGGLESTON—There will be at the end. Taking away the tariffs meant the Australian car industry had to go out and compete in the market; is that not the case? And they did so successfully; would you not agree?

Dr Gruen—At the time when tariffs were being cut the existing owners of the capital complained bitterly that their profits were being eroded.

CHAIR—I will now go to—

Senator EGGLESTON—I have one other question.

CHAIR—All right.

Senator EGGLESTON—There is in place a petroleum resource rental tax from which, I understand, the North West Shelf joint venture is exempt at this stage. Is there any proposal to lift the exemption of the North West Shelf joint venture from the Petroleum Resource Rent Tax?

Dr Gruen—I presume you do not expect me to answer that question, Senator.

Senator EGGLESTON—I simply put it—

Senator Sherry—It is not in the macro group.

Dr Gruen—It is not only that; I do not speculate on government policy

Senator MILNE—I want to ask some questions about Australia's exposure to the ongoing fallout of the global financial crisis, in particular the subprime—

CHAIR—Senator Milne, I am sorry.

Senator Sherry—We cannot hear Senator Milne because of the debate going on.

CHAIR—No, I cannot hear her. If people want to have a conversation, would they please go outside.

Senator CAMERON—Yes, settle down, Barnaby.

Senator MILNE—I remain concerned about Australia's exposure to the fallout of the subprime mortgage crisis in the US and the GFC. I want to know what our vulnerability is in relation to the Future Fund and in relation to any loans that the US Federal Reserve might have made to the Reserve Bank. I understand the Future Fund has a considerable investment in the USA. Can you tell me what percentage of that investment in the US was invested in derivatives or collateralised debt obligations and what losses the Future Fund has incurred because of that.

Dr Gruen—You have a higher estimate of the number of things I keep my head than I in fact do. We can take a question like that on notice. Do you have a copy of the budget with you?

Senator MILNE—No, I do not have those papers here.

Dr Gruen—On page 7-6 there is a table which gives the asset allocation for the Future Fund as of 31 March 2010. The categories are: Australian equities, global equities, private equity, property, infrastructure, debt securities, alternative assets, cash and Telstra holdings. So there is a breakdown there that can at least give you some information about that.

Senator MILNE—Maybe you could just take it on notice for me what percentage of the Future Fund is invested in the US, what was invested in derivatives and collateralised debt obligations, and what your estimate is of any losses to the Future Fund because of that.

Senator Sherry—The questions you are asking go to the Future Fund itself, which appeared in Finance last week. To the best of my recollection, some of the issues you have touched on were put to the Future Fund. But they should definitely go to the Future Fund. Macro do not have responsibility.

Senator MILNE—Could I just ask macro to tell me whether they think we do have ongoing exposure through the other question I asked, which was: did the US Federal Reserve loan the Reserve Bank money which it then loaned on to the banks, and what is our vulnerability about that?

Dr Gruen—My understanding is that there was a swap agreement between the Reserve Bank and the Fed, but we can certainly find out what information there is and get back to you on that.

Senator MILNE—Thank you. I have a question in relation to the G20. At the G20 meeting in Pittsburgh in September last year the Australian Prime Minister signed on to the communique, and there was a commitment to reform fossil fuel subsidies. The ministers there called upon their finance and energy ministers to prepare implementation lines and timetables. I understand there is a meeting in Korea at the end of this week at which there will be a final review of each country's plan for the phase-out of fossil fuel subsidies. I ask Treasury now to table Australia's submission to the finance ministers' meeting in Korea—or to the meeting in Toronto—this week. Can you also tell me whether Treasury, in doing that work, accepts the definition of subsidies that the International Energy Agency or the OECD make, because the

definition of what a fossil fuel subsidy is is going to make a big difference as to what is declared and what is phased out.

Mr Flanagan—The communique established a set of work that has been taken up by a working group. The lead agency for Australia within that working group is actually DRET, rather than Treasury, but we are participating in that working group and, obviously, have the lead in the actual meetings that will be occurring in Busan at the end of this week.

At this stage we are not in a position to table any of the inputs around the G20. As to what information will be released on those various reports, that is usually left as a consideration for the meeting itself and the ministers at the meeting. I can indicate at this stage that this meeting certainly will not be at a point where it will finalise the views for some of the issues you have touched on about definitions and what, indeed, a subsidy is. There are still issues where discussion is going on between different countries as to what the appropriate definition is for subsidy. As I understand it, the report is still very much in progress, and there will not be a resolution of these issues in Busan.

Senator MILNE—I recognise there is a contestability about the definition of subsidy, that is why I asked whether Australia—not what other countries might do, but Australia—accepts the OECD or the International Energy Agency definition of subsidy for the purposes of this international negotiation.

Mr Flanagan—I would have to take that level of detail on notice.

Senator MILNE—If you would not mind; and can you tell me if Treasury has conducted any analysis of subsidies for fossil fuels in Australia?

Mr Gruen—Not in macro group. To the extent that this has been done, it would have been done by an area that was interested in the detail of that industry. So I guess—

Senator MILNE—So who would be doing the work?

Mr Gruen—You could ask that of fiscal group, but I am not sure—it may not be them either. But I would suggest that you ask that question of fiscal group later in the day.

Senator MILNE—On who is doing—

Mr Gruen—Whether they have done any analysis—

Senator MILNE—Done any analysis of the subsidies for fossil fuels, and which ones can be eliminated et cetera.

Mr Gruen—I think so.

Senator Sherry—We will take it on notice: if any work has been done and, if so, by whom. It is certainly not macro—I think we can safely say that. I will come back to you. We will also take on notice—I am not sure which minister, if any, is representing us in Korea; I just do not know—the details of any statements or presentations that are made by whomever is attending that meeting, whether it is a minister or an official. I just do not know at this point in time? Mr Flanagan, do you know the minister?

Mr Flanagan—The Treasurer will be representing Australia, as well as the Reserve Bank governor.

Senator Sherry—The Treasurer is going—

Senator MILNE—They will both be at the Korean meeting?

Mr Flanagan—That is correct.

Senator MILNE—But you cannot tell me anything at this stage about what Australia is submitting to that meeting? I understand that in Pittsburgh there was an undertaking that there would be implementation plans and timelines. Can you at least tell me what the time line is for the phase-out that Australia is agreeing to, or proposing?

Mr Brummitt—The key thing about the time line, and in the context of your remarks about the upcoming meeting in Busan this weekend, is that the next step is the summit in Toronto. Nothing about the fossil fuel issues will be finalised within the G20 ahead of Toronto. That is why there is still a considerable degree of flux around these issues, including within Australia's position and on definitional type issues from a whole range of countries.

Senator MILNE—I understand that this is the beginning of the process and nowhere near the end of the process. What I am trying to get to is that I understood that each country had to put in a report on progress from Pittsburgh to Busan in preparation for Toronto, and that we were expecting Australia to put in a submission as to what our timetable is for phasing out fossil fuel subsidies. Is that not correct?

Mr Brummitt—I have got that here, but I think that—

Senator MILNE—What are we committing to? Why did we sign up to anything?

Senator Sherry—I guess we will know when the minister makes the presentation on behalf of Australia at Busan. We will know at that time.

Senator MILNE—From the point of view of people around this table, who are representing the Australian people, we might have an interest in knowing whether the Australian government is committed to phasing out fossil fuel subsidies. If so, what is the time line that we are proposing to put to the rest of the world? We have a right to know that.

Senator Sherry—Beyond what we have been able to outline so far we will just have to take it on notice. Given the timing of the meeting is this weekend, I do not see that we can do anything but that.

Senator MILNE—I will put it on notice that I would like all the documents that Australia is putting forward in relation to its proposition about what constitutes a fossil fuel subsidy and the time line that Australia is committing to. You can take that on notice because you will have it in a few days time, presumably.

Dr Gruen—I can add something to earlier remarks. You were asking about the Reserve Bank arrangements with the federal reserve. In the Reserve Bank's annual report of 2009, they have a table on page 27 in which they detail the assets and liabilities on their balance sheet. Two of the lines, one in the assets column and one in the liabilities column, are federal reserve swap collateral and federal reserve swap deposit and those numbers were both \$34 billion as of December 2008 but had fallen to zero by the middle of 2009. It is probably the case that if that has changed—I am not on top of the detail—as I understand it, these were swap lines that were put in place at the height of the crisis and have since been unwound.

There has not been any action on this since then. I do not want to make that as a definitive statement but that is my understanding.

Senator PRATT—The KPMG Econtech modelling says that resource investment will increase by 4.5 per cent, resource sector employment will increase by 7 per cent and resource sector output will increase by 5.5 per cent. Can you explain how it is that the RSPT achieves this goal?

Dr Gruen—I am not the expert on this.

Senator JOYCE—That would be a good explanation.

Dr Gruen—I am not the expert on this but it goes to the answer I gave to Senator Eggleston. If you compare an efficient tax with a less efficient one, what you are trying to do is get as close as possible to not distorting the decisions of the private sector. By that economists mean that if you asked the question ‘what would resource allocation look like in the absence of any taxes’, a well-designed tax will move you as little as possible from that position. In other words, the place to start is by asking: what would resource allocation look like in the absence of any taxes?

A royalties tax takes you a fair way from that no-tax world because it puts a charge on the extraction of resources by volume independent of whether or not extracting those resources is profitable. The point there is that there will be mines which can make only a small amount of money from extracting resources. With the imposition of a royalties regime, it becomes a proposition with a negative present discounted value and so you do not do it.

If you can rebate the royalties and instead put in a tax which is less distorting then the outcome can be that mines which were previously uneconomic become economic and you move closer to the world of resource allocation that would exist in the absence of tax. That is the point of the resource super profits tax: to move you significantly closer to the resource allocation that would apply in the absence of tax. So you can introduce a more efficient tax which will generate more revenue and be less distorting. That is the point.

Proceedings suspended from 10.15 am to 10.31 am

CHAIR—We will make a start again. Senator Pratt is continuing.

Senator PRATT—Dr Gruen, thank you for your explanation of the RSPT and why it should benefit the economy. It sounds like a win-win scenario for the economy overall. So why is there such an outcry from certain sectors? Who are the losers in this scenario? It sounds like the whole economy benefits, but at whose expense is that? Is it simply at the expense of those who have to pay a fair price for the resources they are exploiting if they are at the higher end of profit earnings?

Dr Gruen—I am not really the person to give answers about the RSPT. It is obviously the case that, to the extent that more tax is raised, that comes at the expense of shareholders. That is clear. In answer to your question, the tax can be more efficient, but it also means that more revenue comes to the Commonwealth.

Senator PRATT—But, as you outlined before, it should not be at the expense of jobs.

Dr Gruen—The modelling that was done by KPMG Econtech showed the situation in the long run and made the argument that economic output would be higher than without the tax. There should be no implication for jobs in the long run, simply because over an extended period of time the economy can adjust to changes in relative prices and employ the same people—at an aggregate level, not necessarily the same individuals.

Senator PRATT—In terms of the benefits flowing through to the economy, Western Australians are being pushed pretty hard with a scare campaign saying that the tax will hurt them. But, as you have outlined the principles behind this tax, there is no reason to believe that all of these benefits from investment in the mining sector will not flow through to small business across Western Australia.

Dr Gruen—Again, these are all long-run results from the modelling. But they do say that you end up in a world with higher output. As I said earlier in answer to other people's questions, I am not aware of the regional detail of what the modelling shows, so I am not really in a position to comment on that.

Senator PRATT—One of the constraints on the Australian economy is infrastructure. I am interested in your thoughts about tax and how the economy really should be investing to address such constraints, particularly in states that are generating the wealth but our capacity to continue to do that can be inhibited by a lack of investment in infrastructure.

Dr Gruen—You are really asking me questions outside my area of expertise. As I think I said earlier, I need to have a broad understanding of this tax in order to do forecasts on the macroeconomy. Beyond that, I am not really the expert.

Senator PRATT—Fair enough. Thank you, Dr Gruen.

Senator BUSHBY—I thank members of the Macroeconomics Modelling Division for coming along to assist us. I direct you to Budget Paper No. 1, page 2-23, which shows chart A, 'Economic growth and fiscal stimulus' for 2009. On page 2-24 the chart is explained thus:

Chart A shows, for 2009, the relationship between the size of a country's fiscal stimulus and the extent to which economic growth exceeded the IMF's April 2009 forecast.

Those countries that enacted large and timely fiscal stimulus packages, including China, Korea and Australia, performed much better than expected. Those countries with smaller packages, such as the US, Germany, Canada and France, tended to perform broadly in line with expectations. The relationship shown is highly statistically significant, with a t-statistic on the slope coefficient of 3.3.

Why did Treasury only include 11 of the 19 data points that were provided in the source IMF publication?

Dr Gruen—I have a detailed answer to this question, which I am very happy to hand to you. It is long. I will not read it all out, but I will read out the relevant bits. Does it make sense for me to give you one copy of this and also give Hansard a copy?

Senator BUSHBY—You can provide it to the secretariat.

CHAIR—You can table it and it will be distributed.

Dr Gruen—I only have three copies.

Senator BUSHBY—They will make copies.

Dr Gruen—Let me read from this answer. I will table it. I do not need to read the beginning part because it basically follows on from what you have said: It states:

Professor Sinclair Davidson of RMIT has pointed out that, when the dataset includes all 19 countries of the G-20 (rather than being restricted to the 11 countries used for the regression reported ... the estimated slope on the regression line is much flatter, and the coefficient becomes statistically insignificant ...

Professor Davidson is correct. Before publishing the results in the Budget, the regression result for the full sample of 19 countries was checked. Unfortunately ... an error was made and the erroneous conclusion was drawn that the results for the restricted sample did not differ, to any material extent, from those for the full sample.

We have done some more work. It is of interest to report results using samples of countries that are more alike than the wide range of countries in the G20. A common way to do this is to restrict the analysis to OECD countries. That also has the advantage of that more closely comparable data available. We show in this, which I have just handed out, the results if you limit the sample to the OECD members of the G20, but then we also do an analysis where you take the whole of the OECD into account, excluding those countries that were in such dire fiscal circumstances that they were forced to tighten fiscal policy on the grounds that we do not think those countries are relevant to the analysis.

If you do the analysis for the 26 OECD countries which initiated fiscal stimulus, you find that the result that we report is, indeed, statistically significant—namely, countries that engaged in larger fiscal stimulus outperformed relative to those that did less. We have a final summary paragraph:

... there is no statistically significant relationship for the 19 G-20 countries, in 2009, between the size of the fiscal stimulus ... and the extent to which actual GDP growth exceeded the IMF April 2009 forecast. For the more closely comparable 26 OECD countries that applied fiscal stimulus in 2009, however, there is a statistically significant relationship, with those countries that applied more stimulus significantly outperforming forecasts relative to those countries that did less. The US Council of Economic Advisors has arrived at a similar conclusion, using different economic forecasts and different samples of countries.

Senator BUSHBY—So the chart that was in the budget papers is based on an error.

Dr Gruen—No, the chart is correct.

Senator BUSHBY—No, your putting it in there and using it was based on an error, which was that you thought you were not presenting anything different to what the full dataset would have presented. The error was that it did present something different.

Dr Gruen—That is right. We would not choose a sample of countries if we thought that that materially affected the outcome, so we had made a check that when you included all the countries in the sample it did not materially affect the conclusion. Unfortunately, one country was miscoded. We obviously check things many times over, but when we did the check we checked what was there rather than what was not there, if you get what I mean. In the checking process—

Senator BUSHBY—Essentially you are saying that it was not a deliberate thing.

Dr Gruen—No, certainly not.

Senator BUSHBY—You were not deliberately data snooping or whatever they call it.

Dr Gruen—Certainly not.

Senator BUSHBY—It was based on errors behind the scenes that led you to present that in the way it was presented.

Dr Gruen—Indeed. It was based on a check that we did. We did a check to assure ourselves that we were not data snooping, to use the language, so then we were surprised when it was brought to our attention by Professor Davidson—well, he did not write to us but he put it on his website.

Senator BUSHBY—We will come to the OECD chart in a second, but, in respect of the G20 chart, what is in the budget paper could be read as misleading in terms of what it actually represents.

Dr Gruen—I think the facts are clear, so I would not want to put—

Senator BUSHBY—No, that is right, but somebody could read that and draw a conclusion that is not necessarily correct in respect of the G20 countries.

Dr Gruen—It is a conclusion which is not robust, changing the sample of countries.

Senator BUSHBY—So what you have done, as you mentioned, is go off and look at alternative groups of countries—

Dr Gruen—Yes.

Senator BUSHBY—which might deliver the same finding, effectively?

Dr Gruen—The aim was not to deliver—

Senator BUSHBY—Did you look at any other groups of countries, having decided that the G20 was not necessarily the appropriate one even though you selected it initially for publication in the budget paper? Did you look at any other groupings of countries than the OECD as part of your analysis once Professor Davidson had pointed out the problems?

Dr Gruen—We certainly looked at the work that the Council of Economic Advisers had done, and that stands on its own. That uses, I think, a wider range of countries, but it uses a different initial forecast. It does not use the IMF forecasts; it uses JP Morgan forecasts from, I think, late 2008. So there are a range. We simply give the link to that work.

Senator BUSHBY—Did you perform a similar analysis of countries that are primarily commodity-producing countries?

Dr Gruen—No, we—

Senator BUSHBY—You now say—after the publication of the budget, when you selected a different group of countries, that being the G20—that the OECD better represents comparable countries with Australia and that is why you are choosing the OECD now. Certainly there are a lot of things in common between Australia and other OECD countries, but not all of them are commodity-producing countries that have a heavy reliance on China for buying those commodities, with the impact that that may well have had on Australia's economy through that period. I think that, although, yes, there are comparable similarities between Australia and other countries in the OECD, they are not exact and there are other

factors at play. I think that you could also do similar analyses—and I would be interested in knowing whether you have—for other groupings of countries that more accurately reflect the important economic factors that were at play over the last 18 months or two years.

Dr Gruen—The question that the analysis goes to is whether countries that enacted larger fiscal stimuluses did better than expected. To answer your question directly, we looked at the OECD—

Senator BUSHBY—That is the only one you looked at after the G20?

Dr Gruen—No. We checked that the statement that Professor Davidson had made was correct, and it is.

Senator BUSHBY—Yes.

Dr Gruen—So we did not check that G20—

Senator BUSHBY—But then you say, ‘Well, okay, G20 is inconclusive’—I guess—

Dr Gruen—Yes.

Senator BUSHBY—‘in terms of the impact of the stimulus in these particular terms.’ So you have looked at the OECD. Did you look at other groupings of countries when you were looking to find an alternative way of maybe finding the answer you were looking for?

Dr Gruen—I would not put it in those words.

Senator BUSHBY—I am not suggesting that you were trying to find that particular result, but you were trying to find the answer of what the impact might have been. Have you modelled all countries that used stimulus packages?

Dr Gruen—The problem is that you need a source for the size of a fiscal stimulus—the OECD provides such a source and the IMF provides it for the G20—so you are limited.

Senator BUSHBY—And those are the only sources that you are aware of?

Dr Gruen—I am sure you could go country by country and use their own country estimates, but what we and the—

Senator BUSHBY—With varying degrees of veracity and accuracy?

Dr Gruen—Without saying that—

Senator BUSHBY—Yes, but I could say it if I wanted to.

Dr Gruen—I wanted to say that both we and the Council of Economic Advisers took the view that, if you are going to do cross-country work, there are significant benefits in taking the data from a particular source rather than sourcing it from all over the place. So I think it was natural to look at the G20 or the OECD. We thought that it was of relevance to look at this question for the OECD. As I said earlier, had we been aware at the beginning about when you use the full set of G20 countries, we would not have published the result for the 11 countries that we published it for.

Senator BUSHBY—You are looking for your result here, the new one, just of those 11 OECD members who are also in the G20.

Dr Gruen—We tried that, and then we tried the whole OECD. Sorry, let me be completely clear so that there is no misunderstanding. We exclude from that final sample, which you will see there, the four countries in the OECD that were forced to tighten fiscal policy. We do not include those in the sample, and we explain why in a footnote.

Senator BUSHBY—Which four countries were they?

Dr Gruen—Hungary, Greece, Iceland and Ireland.

Senator Sherry—Perfectly understandable, given the recent events.

Dr Gruen—Just to give an example: in the case of Iceland, the financial system collapses in 2008 and the economy collapses in 2009, but it turns out that the outcome in 2009 is somewhat better than was expected. Given the catastrophe that they were facing, in the task of forecasting how they were going to do in 2009 it was pretty clear that they were going to do appallingly, but just how appallingly was not clear. It is a very different question from a country that is functioning properly and is in a position to initiate fiscal stimulus. So we thought that it was entirely legitimate to exclude those countries from the sample.

Senator BUSHBY—But presumably, if they were tightening their fiscal situation, the size of their fiscal stimulus would have been negative, wouldn't it?

Dr Gruen—It would have. There is an interesting debate. If this relationship is linear, which means that negative stimulus reduces growth just as positive stimulus increases growth, then there would be no problem and you could use all the countries. But there is an interesting proposition, which may well be right, which is that, if you are in dire circumstances so that your public finances are in extremis, further fiscal stimulus simply convinces people that you are never going to pay any of it back and it does not stimulate growth. That is the proposition, which seems to me to be a perfectly reasonable one. So there is a suggestion that, when countries are in dire fiscal circumstances, fiscal contraction can actually be expansionary—and that may well be true. The problem is that that would imply that the relationship is nonlinear, and it is hard enough estimating linear relationships, let alone estimating nonlinear ones.

Senator BUSHBY—I have not had a lot of time to analyse this but—

Dr Gruen—No, I do understand.

Senator BUSHBY—but would you think that this analysis would be sufficiently robust to be published in a peer review journal?

Dr Gruen—Given my success in getting things published in a peer review journal, the robustness of one's analysis is only part of the story.

Senator BERNARDI—Conform to the IPCC.

Senator BUSHBY—Once again, as I say, I have not had a chance to have a good look through this and think about it.

Senator CAMERON—You have got to be able to read it.

Senator BERNARDI—That disqualifies you, Senator Cameron!

Senator BUSHBY—Isn't the literature on the impact of fiscal stimulus much more complicated than comparing data points on a scatter graph? There will be in coming years, I imagine, tomes of economic analysis written about what worked and what did not—very in-depth and complicated analysis.

Dr Gruen—I agree.

Senator BUSHBY—The causation and effect of putting some points on a scatter graph is to say, 'This is how it worked.' Can you say emphatically today that the stimulus is the reason for those points creating that line going up?

Dr Gruen—There are very few economic propositions that one can make with absolute certainty, and so I would say that it is a piece of evidence. As you say, there will be—in fact, one can make a stronger statement: there already are tomes being written about the effect of fiscal stimulus. We are learning more about the effect of discretionary fiscal stimulus, and lots of institutions like the IMF and the OECD are contributing to that work. We already know quite a bit about it, hence the three-Ts principle—temporary, timely and targeted.

We already have some principles which lead us to know something about when discretionary fiscal stimulus is likely to work. The only statement I would make about this analysis is that it is a piece of evidence. It does not—

Senator BUSHBY—It is a piece of evidence, but how much weight should this be given in the overall scheme of things as people analyse the effects of stimulus packages through this period? Is it a key or a minor piece of evidence?

Dr Gruen—I regard it as interesting and of some relevance that OECD countries that engaged in larger fiscal stimulus did significantly better than those that did less relative to the forecasts that were made earlier in the year. I think it is interesting and relevant but I would not make the claim that it establishes anything with 100 per cent certainty.

Senator BUSHBY—So maybe informative rather than determinative.

Dr Gruen—Those are your words. I guess the words that I chose were that it was a piece of evidence in favour of the proposition that discretionary fiscal stimulus had a larger effect on growth than the IMF expected it would early in the year, but it is a piece of evidence—that is what I would say.

Senator BUSHBY—Just a final question on this: the forecasts—so these are IMF forecasts for the OECD or OECD forecasts?

Dr Gruen—It says, I hope.

Senator BUSHBY—Source IMF World Economic Outlook. They are IMF forecasts. These IMF forecasts were published in the full knowledge of the stimulus packages of the relevant countries?

Dr Gruen—That is a good question. In most cases the answer would be: it would be in very considerable knowledge rather than necessarily full. The reason I make that statement is: in order to have implemented significant fiscal stimulus in 2009, you had to have begun the process before April. In our case, for example—in the case of Australia—we had packages, as

you know, in October of 2008, December of 2008 and February 2009; those were the big ones. The December one was small.

Senator BUSHBY—They would have been aware of Australia's situation.

Dr Gruen—Indeed. They would have also been aware of many of these countries. If it was the case that the IMF was aware of all of the stimulus, which might be a slight overstatement but nevertheless let us assume that, then this would be suggesting that the stimulus had a bigger effect than expected. That is what you would include. But another possibility, as you say, is that some of this result is a consequence of further stimulus and the fact that that also had a positive effect.

Senator Sherry—You referred early to relevant comparisons to Australia. I think that the most relevant and most interesting comparison is with Canada. It is a similar economy. There are obviously differences, but it is certainly the most relevant of the advanced economies. Canada has a fiscal stimulus of slightly less than two per cent, looking at the original graph, and it made no apparent difference. Australia's stimulus package did make an apparent difference.

Senator BUSHBY—I would suggest that to draw any conclusions out of that—and I would be interested if any of the macro guys think that I am wrong—you would need to do a far greater analysis than just look at those two points. You would need to look at where they started from and look at the composition.

Senator Sherry—I am just looking at the data that we have in front of us in the budget paper and the data tabled. I am familiar with the outcomes in Canada.

Senator BUSHBY—I know that. But you also need to look at where they started from, the composition of their economy and a whole host of factors that would have interplayed in that.

Senator Sherry—Sure. But your reference earlier was about what the most directly comparable country to Australia among advanced economies is. With Canada, sure there are differences.

Senator BUSHBY—I would expect Canada to be in the range of economies that you would include if you were going to do any meaningful analysis.

Senator Sherry—Sure. But I cannot think of any other economy that is closer to ours. They are obviously not identical.

Senator BUSHBY—In terms of the reliance through this period on commodities, I would have thought that Brazil, South Africa and a number of other countries like them would have had some direct relevance as well, but we will not go on to that. One question that is sort of related to that: has Treasury done a similar analysis on the relationship between the stimulus and unemployment?

Dr Gruen—No.

Senator BUSHBY—Is that something that you think would be of value that may well provide interesting evidence as well?

Dr Gruen—It is possible. But countries started from very different places, so that comparison would be more complicated. You could use the change in the unemployment rate over some period of time.

Senator BUSHBY—The main intention of the stimulus, as enunciated by government members on many occasions, was to save jobs. Surely a comparison of the circumstances with unemployment would be quite useful to the extent that this is interesting evidence in terms of the overall debate.

Dr Gruen—We did what we did because I am not sure whether the IMF or another international agency made forecasts of unemployment early in the year. They certainly made forecasts of growth, but I am not just aware as to whether they made forecasts of unemployment. I am not saying that it could not be done.

Senator BUSHBY—I will leave that one with you. Minister, I was thinking about Canada and had an opportunity of 30 seconds or so to run that around in my mind. The fortunes of Canada are very closely linked to the United States, whereas ours these days seem to be far more closely linked to China. The performance of China and the United States throughout the period were very different. That is a glaring and obvious example of why things might be different.

Senator Sherry—There is certainly a North American impact. But with Canada there is certainly an Asian impact as well.

Senator BUSHBY—Absolutely. But the US is far more important to Canada than it is to Australia.

Senator Sherry—There is no doubt about that.

Senator CAMERON—Dr Gruen, this morning I happened to catch an interview with Mitch Hooke, the Chief Executive Officer of the Minerals Council, on Sky. Mr Hooke used words to the effect that Treasury had to get out of its ivory tower and engage in the real world because they do not understand the realities of tax and the effect on the mining industry. How long has Treasury been giving advice to governments on tax?

Dr Gruen—I suspect that Treasury has been giving advice to governments on tax since 1901.

Senator CAMERON—Since 1901?

Dr Gruen—I would imagine—I was not there.

Senator CAMERON—Do you agree with the proposition that you are in an ivory tower and isolated and do not understand the realities—and by ‘you’ I mean Treasury—when it comes to dealing with tax issues?

Dr Gruen—I am not sure that I want to engage in a slanging match with Mitch Hooke. Speaking for the macroeconomic group, part of the process of putting together forecasts involves doing extensive business liaison—in other words, going out and talking to business about how they see the world. We certainly do not simply rely on evidence from our own analysis or from Australian Bureau of Statistics releases. We also look at survey evidence that comes directly from consumers or businesses and we go out and talk to businesses. If you are

asking the question from our perspective, it is certainly not the case that Treasury sits in Canberra and never takes any interest in the fortunes of real businesses or real people. We do that.

Senator CAMERON—There is a website called ‘Keep Mining Strong’, which is, I suppose, the propaganda organ of the Minerals Council. They make a number of assertions, and I would like to test some of those assertions from a macroeconomic perspective. There is a blog that has some prominence on that ‘Keep Mining Strong’ website from Ivor Ries from the Eureka Report. He says:

The Rudd government has been keen to spin the message that proposed Resources Super Profits Tax will not affect how international investors perceive Australia. Rudd also claimed that the recent selloff in the Australian dollar is part of turmoil in global markets. Of course, both assertions are complete bollocks.

He goes on to say:

I’ve run a quick check on the exchange rates of alternative investment destinations and it’s clear that Australia is now being shunned in favour of stable, low-risk investment alternatives such as Mozambique, Thailand and Somalia.

Senator Sherry—I wouldn’t be paying this bloke for advice, I have to say.

Senator CAMERON—He says:

And you can see why. Despite the fact that they are currently engaged in civil wars or that the only growth they are seeing is in piracy, their governments aren’t about to start expropriating the profits of their key export industry.

Maybe because they are too busy fighting pirates and too busy fighting civil wars! This is the sort of rhetoric that is on this website. But there are a couple of important points that have to be addressed. While Mozambique, Thailand and Somalia are out there fighting drug cartels and civil wars, I suppose that they are not going to be thinking about imposing fair taxes. The argument that is put up here is the assertion that the European turmoil has had no effect. He says that to say it has is bollocks. Can you take us to what the view of the macroeconomics group is on that? What has been the effect of the—

Dr Gruen—I have to admit that I do not follow the Somalian currency, so I cannot tell you what has happened to the Somalia currency—or the Mozambique one. I cannot even tell you its name. But let me make some remarks about forces on the Australian dollar. Taking you back to late 2008, in the aftermath of the collapse of Lehman Brothers, there was a big rise in risk aversion—that would be one way of putting it. There was a huge rise in risk spreads all across the financial markets and big rises in risk aversion. One of the ways that that manifested was in falls in commodity prices. Another way that it manifested was in a very sharp depreciation of the Australian dollar.

The Australian dollar is a highly traded currency. One of the things that was observed at that time was that the Australian currency fell by more than the currencies of other commodity exporters—for instance, Canada. In 2008, at a time when global risk aversion was rising strongly, we saw a decline in the Australian dollar that was quite rapid and quite substantial. It was larger than the decline in the Canadian dollar. It is a general proposition

that, when risk aversion rises in global financial markets, commodity prices tend to come down and the Australian dollar tends to come down.

The period since the sovereign debt worries, particularly in Greece but also in other peripheral European economies, has also seen a rise in spreads—nothing like to the extent that we saw in 2007 and 2008 but nevertheless spreads of things like the 90-day bank bill over the overnight index swap or the LIBOR rates over the overnight index swap have risen somewhat. So there has been a rise in risk aversion in global financial markets. There has been some fall in commodity prices. And there has been a fall in the Australian dollar. That pattern is consistent with what happened in 2008, but on a much smaller scale.

Senator CAMERON—I want to get your views on some of the other assertions that are made by the Minerals Council on this website. They ask ‘What does it mean for me?’ for anyone who is reading it. They say:

This is a tax that, if implemented, seriously threatens Australia’s competitiveness, jeopardises future investments and will adversely impact the future wealth and standard of living of all Australians.

It says:

The tax will place ‘additional upward pressure on coal and gas prices, increasing energy costs further’.

That is a quote from Grant King, the Origin Energy managing director. What is the view of the macroeconomics view on those assertions?

Dr Gruen—Dr Henry addressed this question a week ago when he said that a resource rent tax should not put upward pressure on prices. He answered that question. The reasons for that are laid out. The economic analysis surrounding this tax is laid out in the Henry tax review, so I do not think that I need to add to that.

Senator CAMERON—Another proposition on this part of the website is that interest rates could rise. They quote the financial commentator Terry McCrann saying that what is being proposed is ‘nationally suicidal’. Is there any evidence to back up this observation from Terry McCrann?

Senator BERNARDI—The fact that interest rates have been rising is one.

Senator CAMERON—This is about interest rates rising because of the superprofits tax.

Dr Gruen—I do not see the link. It is not clear to me why interest rates would rise as a consequence of the resource superprofits tax. I do not comment on suicide.

Senator CAMERON—There is another proposition on the same Minerals Council website. It says:

The tax could weaken property markets, impacting on the value of your home or property investment.

Was there any analysis done on this?

Dr Gruen—Again, I do not see the link. I have not seen analysis by Terry McCrann or anyone else explaining that link.

Senator CAMERON—It goes on to say that it means more money for other countries and less for Australia. Is there any evidence that that is a valid proposition?

Dr Gruen—Given my answers to previous questions, no I do not think so.

Senator CAMERON—One of the other assertions is that the shareholder or superannuant says the mere announcement of the government's super tax on resources wiped billions of dollars off the value of those shares in just one week. Is there any evidence that that is a correct statement?

Dr Gruen—We have certainly had a look at resource prices in Australia and compared them with other countries, and the broad conclusion we draw is that resource price indexes in Australia have fallen pretty much in line with declines in commodity prices, as measured on the London Metal Exchange, and that if you take a broad aggregate of Canadian, US and Brazilian resource companies they have also fallen roughly the same, with a pattern that looks very similar. In other words, both indices have fallen roughly in line with declines in commodity prices as measured on the London Metal Exchange. I should add, these are simply broad patterns. One would expect some effect from the resource profits tax on share prices, but there are a lot of other things going on and those things are quite important. So declines in commodity prices have always had a very profound effect on resource share prices, understandably.

Senator CAMERON—The Minerals Industry Council, on this website, has a question: what is the tax? And they ask: what is a super profit? They say:

From the name, 'Super Profit', you would think the new tax targets only very large profits.

In fact the tax targets any profit that's more than 6 percent - or about the return anyone could make from a term deposit at a bank.

So the name 'Super Profit' is misleading because it suggests it is only targeting excessive, windfall profits. In reality it will hit normal profits—not just 'super profits'.

Is that an accurate statement?

Dr Gruen—I think Dr Henry has dealt with this in his ABE speech and it is certainly not the case that the tax applies only to profits above the government bond rate. The relevance of the government bond rate is to do with what is an appropriate discount rate to use for flows of income through time that are certain. But this is all dealt with, in some detail, in Dr Henry's speech to the Australian Business Economists—I think a week after the budget—where he goes through an explanation of why it is the case that the use of the government bond rate in the resource super profits tax is not the rate beyond which tax is applied.

Senator JOYCE—Do you know what the federal government's gross debt is?

Dr Gruen—I can put my hand on it—I will let you go ahead, it is just that this is really the fiscal group's area of expertise. It depends on what we are talking about.

Senator JOYCE—It is about the analysis.

Dr Gruen—If you have not seen the budget papers, I presume this is the number.

Senator JOYCE—What is the gross?

Dr Gruen—Total interest-bearing liabilities as of 2009-10—that is presumably still a forecast—

Senator JOYCE—It is.

Dr Gruen—It is table 2 in statement 9, and the number for 2009-10 is \$166.6 billion.

Senator JOYCE—What are the states' debts at the moment?

Dr Gruen—These are questions you should address to Fiscal Group.

Senator JOYCE—Why in budget papers does Treasury only present net debt data for the Australian government general sector whereas other countries are presented as total government debt?

Mr McDonald—I believe that if you go to Budget Paper No. 3 there are tables at the back of that that present both gross and net debt based on the Australian government, state and local government, and public corporations. Those are questions that the commonwealth and state relations division of Fiscal Group would be able to address in further detail, but that data is presented.

Senator JOYCE—If other countries broke up their debt into 15 different components they could end up with a low debt at a federal level, but it is not really the case, is it? You have to look at the total debt of all your sectors that are under the auspices of the term 'government'.

Dr Gruen—It depends on which question you are interested in answering. The Commonwealth government's balance sheet is obviously something upon which the Treasury reports, and that is obviously something that is of considerable relevance. There are many federal systems out there and, as Mr McDonald said, the data that you are talking about are in the budget.

Senator JOYCE—If, for instance, a state in Australia were unable to repay its debt, what would happen to the state?

Dr Gruen—I think, again, it is best to address these questions to Fiscal Group.

Senator JOYCE—Fair enough. Treasury included state government debts in its publication entitled 'A history of public debt in Australia'. I saw that on page 5. If you could do it for Treasury staff papers, why can we not do it for the budget papers?

Dr Gruen—I think the best thing to do is address this question to Fiscal Group.

Senator JOYCE—I will go back to monetary policy in that case. Is there a trade-off between fiscal and monetary policy?

Dr Gruen—There can be a trade-off, certainly.

Senator JOYCE—There 'can be' or 'generally is' a trade off?

Dr Gruen—Give me a specific example and I will try to deal with it.

Senator JOYCE—If I jam a heap of money into the economy and stimulate it, will it have inflationary pressures?

Dr Gruen—The answer to that question depends very much on whether there are unemployed resources in the economy. If you were to engage in fiscal expansion at full

employment then that fiscal expansion would be crowded out by a combination of higher exchange rates and higher interest rates as applied by the central bank. So if you were to engage in discretionary fiscal stimulus at a time of full employment then the implications of that would be that monetary policy would likely offset it with higher interest rates. It is worth drawing the distinction. In a situation as we faced in late 2008 and 2009, when there was a very substantial retreat in private sector demand, both fiscal and monetary policy were acting extremely quickly to try to offset that decline in private sector spending, so they were both acting in concert to limit the extent of the economic downturn.

Senator JOYCE—But there is still a form of stimulus expenditure going on right now.

Mr Gruen—It is certainly the case that the packages that were put in place in 2009 have a profile of spending which continues at present, as you say. But it is relevant to make the point that if you are looking at contributions to growth the fiscal stimulus made a substantial economic contribution to growth from the December quarter 2008 and through 2009. Our estimates are that fiscal stimulus will subtract one per cent from growth in 2010 and three-quarters of a per cent in 2011.

Senator JOYCE—We are currently borrowing money from overseas right now to pay for things that are part of a stimulus package, such as the Building the Education Revolution and pulling ceiling insulation out of roofs. So we are still currently spending money that was earmarked for stimulus purposes, and we are borrowing the money from overseas. The question is, should we be doing that if we are also jacking up interest rates?

Mr Gruen—I guess we need to go back a little bit. At the time when the economy was weakening, both fiscal and monetary policy were employed to try and support the economy. So interest rates were cut very substantially from 7.25 down to three, and fiscal expansion was put in place. Now, there is an important difference between fiscal and monetary policy which is worth keeping in mind in trying to think about this. When you put in place a fiscal stimulus package, you commit to spending and transfers over a particular period. If nothing else changes, if you then do not touch anything, that stimulus goes away because the spending is made, it has an effect on the economy and then the spending gradually declines. The effect on the economy is that in the short run you make a contribution to growth and then as the stimulus is being withdrawn it gradually detracts from growth. That is different from monetary policy. If you cut interest rates to three per cent, you need to bring them back up again in order to generate the same effect as you do with fiscal policy. In other words, to get a stimulatory effect in the short run and then to withdraw that stimulus requires that you cut interest rates, keep them there for a while and then bring them up again. So fiscal policy by the way it is designed has both the early stimulus and the later detraction from growth built into the design. In the case of monetary policy, in order to replicate that feature you need to cut interest rates and then put them back up again. So both monetary and fiscal policy were contributing to growth from late 2008 till about the end of 2009 and now they are both subtracting—well, monetary policy is actually probably not subtracting from growth yet but fiscal policy is.

Senator JOYCE—So you are saying that the money they are spending on the school halls is detracting from growth at the moment.

Mr Gruen—It needs a slightly longer sentence. To the extent that you spend less, let us say in 2010, than you spent in 2009, that detracts from growth. That is the relevant thought experiment. My colleague has just reminded me that the way to think about it is that the spending continues to contribute to the level of GDP but it is detracting from the growth rate. I hope that is helpful.

Senator JOYCE—So what do you think is happening in the economy now?

Dr Gruen—A lot of things.

Senator JOYCE—But what in particular? Do we need to be spending money to stimulate the economy, or should we be slowing the economy down because it is becoming inflationary?

Dr Gruen—I think it is appropriate for fiscal policy to be detracting from growth, at present, because I think the whole design of these packages was to support the economy when the private sector was in retreat. Now that private spending is recovering it is appropriate for fiscal policy to be gradually withdrawing the stimulus, and I think that is what is being done.

Senator JOYCE—Why do we have to have this gradual withdrawal? Basically, if we are getting touched with the money we are spending anyhow—and that is becoming completely evident; we are paying way over the market for what we are getting, and up to 300 per cent on what the actual costs should be—instead of throwing this money away, why don't we just stop spending it?

Dr Gruen—I am not going to comment on the efficacy or otherwise of the spending; it is not my place to do that. But the general macroeconomic proposition that you would design a package which contributes to growth when the economy is weak and then gradually reduce that stimulus I think is best practice. I do not think anybody recommends that you build up the stimulus and then just stop it immediately, because I think that would have a very substantially deleterious effect on economic outcomes. To give you an example: the cash payments that were paid in December 2008 and over a few months in 2009 had a very noticeable effect on retail trade, and as that effect has faded retail trade has become quite soft. So the point is that there are signs in the economy already of the effect of the withdrawal of stimulus. If you look at the estimates for the budget underlying cash balance it is a pretty rapid withdrawal, which of course takes into account not only the ending of the discretionary stimulus but also the improving state of the economy. So the automatic stabilisers are in there as well. Nevertheless, if you compare the rate at which the underlying cash balance is forecast to improve, it is a lot faster than coming out of either the early eighties or early nineties recession. So I think what I would argue is that the timing of the fiscal stimulus this time around was significantly better than it was in the previous two big downturns that we had, and that it is being withdrawn at a reasonably rapid pace.

Senator JOYCE—I have got a problem with that statement. When you say we are withdrawing it, why on earth, if that is the case, have we moved forward all the capital expenditure on such things as roads—I think, at one point, \$5 billion of it—from almost one and two and, in some cases, possibly three years out, into this current year?

Dr Gruen—If I understand your question, when I say withdrawing I guess what I am saying is: to the extent that you, in year 1, spent a certain amount of money and then in year 2

you spent less, that would stimulate the economy in the first year. Then, in the second year, it would continue to have an effect on the level of real output, but that effect would be smaller than in year 1, and therefore it would be detracting from growth; I think that is all I am saying.

Senator JOYCE—But what we have actually done seems counterintuitive to what you have told us. What the government has done is to reach forward into the future years, grabbed expenditure on such things as the Ipswich Motorway, payments to local councils and a whole range of other projects and moved all the payments into this year. If we are trying to withdraw from stimulus, that is doing completely the opposite; that is turbocharging stimulus.

Dr Gruen—You have to add it all up. You have to take into account the full package of measures and then ask the question—which is what we do when we are putting together our macro economic forecasts. We make an assessment of how much each of the different measures will stimulate growth in output and we also put together an estimate of over what time period they will have an impact. We add them all up and then we ask the question: in aggregate what are these packages doing to the level of output through time? As written in the budget, in statement 2—I will just refer to the numbers—our assessment is, based on our estimates of the effects of the total fiscal stimulus package, that through 2009 they contributed two per cent to growth, through 2010 they are going to subtract about one per cent and through to 2011 they are going to subtract about $\frac{3}{4}$ per cent. They are continuing to contribute to the level of output; they are just reducing its growth rate.

Senator JOYCE—Why would we have a budget position that, two years ago in the middle of the global financial crisis, put forward payments on capital expenditure projects and now, when we get the statements—even by Dr Henry, who says that as far as Australia is concerned the global financial crisis is over—we would therefore reach forward to predict expenditure projections that we made in the middle of the financial crisis? And now that we are out of the financial crisis, so Dr Henry tells us, we are reaching forward, grabbing those payments and putting them into this year?

Dr Gruen—I am not certain what you are referring to.

Senator Sherry—I think he is effectively recycling an earlier question, which I think was answered, to the extent that the details in the earlier question were the responsibility of the macro group. The macro group does not have detailed knowledge of particular construction or highway projects that you were referring to.

Senator JOYCE—If we go to Budget Paper No. 2 page 172, there is a section that talks about roads.

Senator Sherry—What page was it again?

Senator JOYCE—I was given page 172, but I do not think that is it.

Senator Sherry—This is budget measures. I have ‘Adventure playgrounds’ and ‘Bulk verification of community housing rent’. Is that where you want us to go to?

Senator JOYCE—That is not the one.

Senator Sherry—I am sorry, but I have just been told—

Dr Gruen—Do you want the Ipswich Motorway?

Senator JOYCE—Yes, the Ipswich Motorway. What page is that on?

Dr Gruen—272.

Senator JOYCE—At page 272 you can see that the nation building programs were moving all these payments forward—for example, Ipswich Motorway. Those predictions were made when the financial crisis was on. Now that the financial crisis is off, we are moving the payments into this year and creating a stimulatory effect, which is an inflationary effect, which puts up interest rates. Why would we be doing that?

Dr Gruen—I am not going to give an answer in particular about the Ipswich Motorway because I do not know that level of detail. If you want that level of detail you would need to talk to the fiscal group. But I can certainly answer the kind of general proposition. The general proposition goes to the chart that I was talking about earlier in statement 2 of Budget Paper No. 1, which simply summarises Treasury's view of what the total effect of the stimulus packages is when taken as a whole—adding up all the pieces, including the cash payments, the Building the Education Revolution and various other pieces of it—

Senator JOYCE—Marvellous bits of work.

Dr Gruen—You are going to ruin my train of thought, Senator.

Senator CAMERON—Senator Joyce, I am in charge at the moment so just behave yourself.

Dr Gruen—So the—

ACTING CHAIR interjecting—

Senator Cameron interjecting—

Senator Sherry—You are interrupting the witness's train of thought very definitely now. Please, give him a go.

Dr Gruen—When we do that based on all the measures in this budget and all the measures that were announced previously, our assessment is that fiscal policy is contributing, as I said, two per cent to growth through 2009. It also made a contribution in 2008 but nevertheless that is the situation in 2009 and then subtract about a per cent in 2010. So the turnaround, if you like, in its effect on growth between 2009 and 2010 is three per cent of GDP. It is a very substantial turnaround. You could argue that you would like to see an even bigger turnaround. I think, if you make this turnaround big enough, you will stall the economy and that is the reason for wanting to do this at a measured pace.

Senator JOYCE—It is all very confusing that in the time when the financial crisis was on we had projections of the expenditures that went out. Now the financial crisis is over and we should be reducing the stimulatory effect rather than do that we have gone and found \$1.5 billion worth of expenditure and jammed it in this year. I put to you this question: it has nothing to do really with a desire to affect inflation or interest rates or an observance of monetary or fiscal policy, this has everything to do with the government bodging up the figures to make the highest baseline possible for their two per cent expenditure commitments.

They put that priority way above any of their diligence to look after monetary or fiscal policy or the effects on the economy.

ACTING CHAIR—Senator Joyce, there is a point of order from Senator Cameron.

Senator CAMERON—The point of order is that Senator Joyce cannot ask Dr Gruen to speculate about the government's position on this. It is not his position to speculate. It is a hypothetical question and it is not in order.

ACTING CHAIR—It is up to the minister presiding to say that.

Senator Sherry—It is actually not but I had intervened anyway because you were allowing what was a polemic political statement or argument totally devoid of any coherent concise question to ramble on—

Senator JOYCE—That is your opinion.

Senator Sherry—That is my opinion and it is true.

Senator JOYCE—Everybody understands it completely. Have you bodgied up the books just to get—

Senator Sherry—Dr Gruen has already responded to the same question on two previous occasions. What you have done on this occasion with your third attempt at a so-called question is to add a whole range of political argument and rhetoric. If you want to waste the time of the committee that is up to you but Dr Gruen will not be responding to political argument and rhetoric. He will respond to questions.

Senator JOYCE—No, he had responded. We are talking about the stimulus—

Senator Sherry—He has already responded to the same issue on two occasions already.

ACTING CHAIR—Thank you, Minister. Perhaps we could ask Senator Joyce to refocus his question.

Senator JOYCE—I refer to a Treasury staff paper titled 'The effectiveness of fiscal policy in Australia—selected issues' written by Blair Comley, Stephen Anthony and Ben Ferguson. Are you aware of this paper?

Dr Gruen—Yes I am.

Senator JOYCE—This paper investigated the 10-year bond rate real interest margin between Australia and the United States. The paper concluded:

The results suggest that a deterioration of the headline balance of one per cent of GDP is associated with an increase in the margin of around 20 basis points in the short run ...

The paper further concludes:

... an increase in public debt of one per cent of GDP is associated with an increase in the margin of around 15 basis points in the long run.

Would you generally accept the broad directions of this paper's conclusion?

Dr Gruen—We have taken another look at that paper with the benefit of further data. We find that when you update that paper the short-run effect becomes statistically insignificant and the longer run effect becomes smaller. It is obviously a question that we have

considerable interest in. It is a question that is interesting a lot of countries at the moment. I would draw your attention to an IMF staff paper from November 2009 just so that you or your staff have a chance to look it up. It is titled 'The state of public finances cross-country fiscal monitor: November 2009' and is produced by the IMF. That comes to broad conclusions which I think are a little smaller than the ones that that Treasury paper came to. Nevertheless, it comes to the conclusion:

An increase in the overall fiscal deficit of 1 percent of GDP pushes up bond yields by about 20 basis points over the medium term.

They have a range of other conclusions, some of which are certainly of interest. For instance, if you have a large initial high stock of debt then the effect can be bigger; if you have a large initial deficit, the effect can be bigger. There is a range of things that can make the effect bigger.

The other point that they make, which I think it is extremely important, is that these effects are effects that you would expect to see over an extended period of time, and they are not effects that you would expect to see at a time when there is a huge amount of excess capacity in the global economy. So let me just flesh that out a little bit, because it is quite important. There has been, as you would be aware, a very substantial deterioration in fiscal positions of most of the advanced world, so there have been very big increases in fiscal deficits across the developed world and in debt levels.

Senator JOYCE—Believe me, Dr Gruen, I am aware of that more than most people.

Dr Gruen—Indeed you are. If you were to simply apply these rules of thumb then that would lead you to the conclusion that bond yields across the world should have gone up very substantially. In fact, if anything, in the advanced economies, putting aside the ones where solvency is becoming an issue—the peripheral European economies—in Germany, the UK, the US, Japan the bond yields in those countries have come down. Bond yields in Germany are currently the lowest they have been since the 1920s despite the very big increases in debts and deficits.

The point is, the reason I am expanding on this in some detail, is that at a time when there is a great deal of spare capacity in the global economy, or in other words at a time when the private sector has retreated very substantially and has raised its savings and reduced its investment, the big increases in government spending and big increases in government deficits have had almost no impact at all on long-term interest rates. So the results that you get out of these econometric studies, whether you are talking about the Comley et al one, or the ones from the IMF, those are results that you would expect to apply in the medium to long run when the private sectors have recovered.

The point of all of that is that it is therefore important for fiscal consolidation to occur at the same time that the private economies are recovering. That is precisely what is happening here, and is also what is happening increasingly around the world. Some countries are doing their fiscal consolidations earlier than others, but there is no question that if these levels of debt and deficit were allowed to continue into the indefinite future, they would have very substantial impacts of the sort that you have been talking about on long-term interest rates.

They are just not having those effects now because of the huge amount of spare capacity in the global economy.

Senator JOYCE—There are so many more questions that that answer leads to. On the trajectory of debt that Australia is on at the moment, which is between \$1¼ billion and \$2 billion extra a week—

Senator Sherry—Which debt are you referring to? Government debt or—

Senator JOYCE—Gross government debt.

Senator Sherry—Gross, not net?

Senator JOYCE—Not net.

Senator Sherry—Not net, it is gross. Okay.

Senator JOYCE—Your debt, Nick. The debt you are borrowing from overseas.

Senator Sherry—Just for the record, we had gross government debt three years ago. We were borrowing overseas three years ago when you were in government, which I have to say surprised some of your colleagues when I informed them of that fact.

Senator JOYCE—Now between the state Labor governments and the federal government we are about \$300 billion in debt. If we keep borrowing money like that, Dr Gruen, are we going to put upward pressure on interest rates?

Dr Gruen—The statement that I was making was that as the private sector recovers, it will be important for—I guess the measure that I would look at the first would be the measure of net debt as a proportion of GDP, because I think that is a more comparable way to—

Senator JOYCE—In doing that, can you explain for the purpose of the *Hansard* what makes up net debt?

Dr Gruen—Net debt is—

Senator JOYCE—Start with what the gross debt is, then list the items that are going to come off it to come to your net debt.

Dr Gruen—Sure. My colleague has helpfully given me the—

Senator JOYCE—Just tell me the big ones.

Dr Gruen—It is the sum of deposits, government securities, loans and other borrowings minus the sum of cash and deposits, advances paid and investments, loans and placements. So it takes off—

Senator JOYCE—Give me an example of what sorts of things are.

Dr Gruen—That you take off?

Senator JOYCE—Yes, so we can identify them in the budget. What would we be looking at? What would be the sorts of things we would be taking off to come up with a net figure?

Dr Gruen—For instance, you would take off the debt-like instruments that the Future Fund holds.

Senator JOYCE—Ah, the Future Fund! Now what is the Future Fund there for, Dr Gruen? What is the Future Fund there to pay for?

CHAIR—Senator Joyce—

Senator JOYCE—No, this is a very important question: what is the Future Fund there to pay for?

Dr Gruen—The Future Fund, as it was set up, is designed to fund the liabilities from public sector superannuation from 2020 onwards.

Senator JOYCE—So we are going to pay our debt with public superannuation money, are we?

Dr Gruen—Sorry, I did not follow that.

Senator JOYCE—So when you were netting it off, there is a presumption that we would be paying our debt with public superannuation money?

Dr Gruen—No, there is not. There is a presumption that you follow the accounting rules as applied by—

Senator JOYCE—This is very—

CHAIR—Senator Joyce, I think there will be—

Senator Sherry—Senator, the treatment of the assets in the Future Fund under this government is no different from the treatment of the Future Fund assets under the previous government. It has been totally consistent; the definition is totally consistent—

Senator JOYCE—What other things—

CHAIR—Senator Joyce, I think you will have time to follow this up later. Senator Boswell has been waiting a while.

Senator BOSWELL—You would be aware of other modelling and critiques of your modelling for complementary policies for greenhouse gas emission abatement and the national regional employment consequences. A report from the Australian Conservation Foundation and the Australian Council of Trade Unions, prepared by the National Institute of the Economic and Industry Research states:

Whether Australia continues to avoid the need for financial reconstruction is the elephant in the room and the current structural weakness in the Australian economy could generate a balance of payments crisis at any time over the next decade.

Is the ACTU correct in painting this very alarming picture?

Dr Gruen—I was not sure what the structural weakness was that they were talking about. Could you explain it?

Senator BOSWELL—I will repeat the question. The Conservation Foundation and the Australian Council of Trade Unions, in a report prepared by the National Institute of Economic and Industry Research, states:

Whether Australia continues to avoid the need for financial reconstruction is the elephant in the room and the current structural weakness in the Australian economy could generate a balance of payments crisis at any time over the next decade.

Do you—

Dr Gruen—Okay, I think I understand. Without having read that report, I presume that what they are talking about is that Australia for a long time has been running a current account deficit, and it is certainly the case that Australia has run a current account deficit every year, with odd exceptions, for a very, very long time. I think the last time we ran a current account surplus was 1971 or 1972. It is also true that the current account deficit, as a share of GDP, since the mid-eighties has been of the order of 4½ to five per cent of GDP on average. Another way of saying that is Australia has been investing more than it saves; as an economy, we have been investing more than we save for a very long time. I would not necessarily call that a structural weakness. It means that it makes sense for us to keep our public finances in order and it is important that we have effective regulation around the flows of income that go in and out of the Australian economy.

Senator BOSWELL—So you do not think it is an alarming picture from the ACTU?

Dr Gruen—Without further information, I am not certain what they are talking about, but if they are talking about the fact that Australia has run a current account deficit for a very long time then that is true and I think it is something that needs to be watched, but I do not think it is a sign of a balance of payments crisis any time in the next decade.

Senator BOSWELL—The report also states:

An increasing balance of payment deficit raises the question of finance. Will overseas lenders be willing to continue their present high rate of lending to the Australian banks?

Is this a legitimate concern expressed by the ACTU?

Dr Gruen—When it comes the financing of the banks, there is no question that the banks do do a lot of offshore borrowing. There are a couple of things here. Firstly, they swap it back into Australian dollars so that the banks do not have a currency mismatch, a currency exposure. The fact that that is in place has been tested on many occasions when the Australian dollar has moved by large amounts, and it is very clear that that those hedging practices do indeed insulate the banks from foreign exchange fluctuations. The other part of that is that, as a consequence of the global financial crisis, the banks have been moving to source a larger proportion of their offshore borrowings in longer term borrowings rather than shorter term ones. So the banks are taking steps to improve the resilience of their offshore borrowings.

Senator BOSWELL—But is it a concern to you or do you think it is overstated?

Dr Gruen—I think the fact that Australia borrows a substantial amount in offshore markets through the banks is something that means that we need to remain vigilant about the quality of our financial regulation. I think that is absolutely true. Our financial regulation performed extremely well in the financial crisis, but there is no question that the fact that we borrow a lot in overseas markets means that it is extremely important for the Australian economy that we keep the confidence of those markets. That requires sensible domestic policies and good financial regulation. I do not think it is something that is alarming, but I do think it is something that requires that we continue to have sensible policies in this country, particularly in financial regulation.

Senator BOSWELL—The technical report of the ACTU says:

If it does not come to an end from household debt saturation, the Australian boom from 1993 to date could easily end in a crisis in financing the balance of payments deficit.

It sounds like the ACTU has got a bit in common with you, Senator Joyce. They are concerned too. The report goes on:

This would rebound on the household sector by raising prices, through the increased costs of imported consumer goods due to the devaluation and by raising interest rates as well. The resulting fall in household incomes would reduce demand and generate unemployment.

Is the ACTU correct in saying that Australia faces rising prices, rising interest rates, lower incomes and higher unemployment?

Dr Gruen—From a balance of payments crisis?

Senator BOSWELL—The question I asked was ‘through the increased costs of imported consumer goods due to the devaluation and by raisings of interest rates as well’.

Dr Gruen—As I understand the question, it is that the long run of substantial current account deficits is going to lead to a balance of payments crisis sometime in the next decade and that that would have very substantial deleterious effects on the Australian economy. I think I have answered this question, in the sense that there are very understandable reasons why Australia has a high level of investment. Our level of savings is not actually low by OECD standards. In fact, it is almost exactly the average of the OECD. In distinction from a lot of other countries that run large current account deficits, many countries in the OECD do so because they have low savings, and that would apply to the United States amongst others.

Senator BOSWELL—I am asking you—

Dr Gruen—I know you are, and I am saying that I think that the constellation of investment and savings in Australia, which is what is lying behind the large current account deficits, is a consequence of the strengths of the Australian economy—namely, that we are a resource rich country with resources that are in substantial demand from the rest of the world.

Senator BOSWELL—But are we going to face rising prices, rising interest rates, lower incomes and higher unemployment?

Dr Gruen—No.

Senator BOSWELL—No. Thank you.

CHAIR—Senator Boswell, I think it would be useful for the rest of the committee if you could table that document.

Senator BOSWELL—I cannot, because I do not have it. But I certainly will; I will go and get it. The ACTU—

Senator Sherry—Sorry, Senator, but it takes longer than necessary and it is a little difficult if we do not have the document with us.

Senator BOSWELL—I am sorry; I will get you the document. I have got two questions to ask and then you will not need the document—but I will go and get it for you. In the ACTU-ACF report, they model their preferred option of reducing carbon emissions by 50 per cent by 2030. They judge that the ratio of household debt to gross disposable income will stabilise at

around 200 per cent. What would be the implications if we tried to reduce carbon emissions by 50 per cent? This is your mob, Doug.

Dr Gruen—As you know, Treasury did some modelling about what would be the economic implications of reducing carbon emissions over an extended period, and I think we have been through that on many occasions. I think the report on the economics of introducing emissions trading talked about what the economic implications would be of deep cuts in carbon emissions over an extended period of time. The answer to that was that, for most of the scenarios that were looked at, it meant that average growth was slower by 0.1 per cent per annum.

Senator BOSWELL—Per what—one per cent, two per cent?

Dr Gruen—Sorry? It reduced GNP per capita growth by 0.1 per cent per annum for the scenarios that were modelled by the Treasury.

Senator BOSWELL—But that was a five per cent reduction. What would 50 per cent do?

Dr Gruen—It rounds to the same number, if my memory is correct. But Mr Ewing will know this—

Mr R Ewing—I was not entirely certain what time period the 50 per cent was referring to?

Dr Gruen—Yes, it will depend.

Senator BOSWELL—I am quoting the ACTU and ACF report. Their preferred option for reducing carbon emissions was by 50 per cent—

Dr Gruen—By when?

Senator BOSWELL—by 2030.

Dr Gruen—Okay. Well, that is a deeper cut than would have been modelled in our modelling.

Mr R Ewing—I do not have the exact figures to hand. We probably have numbers in that broad area, as the Garnaut minus 25 scenario had a 25 per cent reduction from 2000 levels in 2020, which then went on to a 90 per cent reduction by 2050, and in that case the figure that Dr Gruen quoted is the case: it was a reduction in growth of 0.1 per cent per annum, I believe, in GNP.

Senator BOSWELL—Okay. So you think it will reduce GDP by 0.1 per cent?

Dr Gruen—The growth rate.

Mr R Ewing—Annual GNP growth by 0.1 per cent. The total impact on GNP would be different.

Dr Gruen—Of course, this depends on imposing a carbon price and therefore the reductions being on the minimum cost basis.

Senator BOSWELL—What would the carbon price go to, then, if the 50 per cent reduction by 2030 was implemented?

Dr Gruen—Sorry, Senator, we have not done that particular scenario, but you could certainly find out the carbon price for the Garnaut minus 25 scenario that Mr Ewing was talking about. That would have been in the report.

Senator BOSWELL—Mr Ewing, would you have any idea what that was, off the top of your head?

Mr R Ewing—In what year would you be interested in the carbon price?

Senator BOSWELL—2030.

Mr R Ewing—I do not have that figure to hand, I am afraid. I will have to take that on notice.

Senator BOSWELL—What figures have you got there?

Mr R Ewing—I have 2020 and 2050.

Senator BOSWELL—Give us both, then.

Mr Ewing—In the Garnaut 25 scenario we had an emissions price in real 2005 Australian dollars of \$60 in 2020, which was increasing to \$197 in 2050. If you did the maths you could work 2030 from that, I just do not have that figure in front of me.

Senator BOSWELL—I am sure you could do that for us, as you are more qualified than I am.

Dr Gruen—We will take it on notice.

Senator BOSWELL—They say that requires an assembly of large resources to decarbonise the economy such that by 2030 an extra \$463 billion will have been invested. Can Australia stay afloat while investing nearly half a trillion dollars in decarbonising the ACTU way? What would the consequences be of investing \$463 billion in decarbonising Australia?

Dr Gruen—I would need to see the detail to be able to give a coherent answer to that question. Even without decarbonising the Australian economy we are looking at very strong investment over the next several years as a consequence of our expectation and many people's expectation that China's and India's growth will continue and they will continue to have high demand for the sorts of raw materials that Australia produces. As a consequence of that we are likely to see a combination of substantial mining investment and substantial demands on infrastructure. We are likely to see a run of years in which Australian investment is high by historical standards. It may well be that we are looking at an extended period of larger than usual current account deficits. That is certainly possible.

Senator BOSWELL—I do not think that is the question I asked. What I suppose I am asking, to put it more indirectly, is: what would be the impact of taking \$463 billion out of the economy and investing it in decarbonising the economy, renewable energy and so forth?

Dr Gruen—It would not be taking it out of the economy ; it would be changing the structure of the economy to do some things that it does not currently do and do less of the things that it does currently do.

Senator BOSWELL—Can we afford to spend \$463 billion, in the opinion of the Treasury generally?

Dr Gruen—As I said, I have not seen the report so I am not sure exactly where the number comes from.

Senator BOSWELL—It comes from the report of the ACTU and the ACF.

Dr Gruen—As we said, if you do this in the least-costly way possible, which involves a carbon price, then the cost of even quite deep cuts can be quite small provided you do it over an extended period of time.

Senator BOSWELL—We are in 2010 now so this is in 20 years time.

Mr Ewing—I want to make 100 per cent certain I am looking at the right thing. You are referring to the National Institute of Economic and Industry Research report that was sponsored by the ACTU and ACF, is that correct?

Senator BOSWELL—Yes.

Mr Ewing—I would hate a report that Treasury commissioned to be labelled as Treasury analysis in every instance. I am sure that the ACTU and ACF do not necessarily sign up to every single detail in this one so I just want to clarify that.

Senator BOSWELL—I am not suggesting that you had any involvement in this report. I am just asking your opinion of the report.

Dr Gruen—As I said, I have not had a chance to read it so I am not really in a position to comment.

Senator BOSWELL—Mr Ewing seems to have.

Mr Ewing—Yes, I have a copy in front of me.

Senator Sherry—Not a hard copy, it is the wonders of new modern technology that he is accessing.

Mr Ewing—But I should also clarify that, unfortunately, I was on leave when this report came out so I am looking at aspects of it for the first time now.

Senator BOSWELL—It seems a significant, a huge amount of money, \$463 billion, to be spent by 2030 to decarbonise Australia.

Dr Gruen—I think we may well have said all that we can usefully say. We made the point that if you were to do this at the lowest possible cost, which involves a carbon price, the costs would be the ones that I reported earlier and you could engineer deep cuts in carbon emissions provided it is over an extended period of time and provided it is done using market mechanisms.

Senator BOSWELL—What would the impact on the economy be?

Dr Gruen—As I said, for the scenarios that we looked at, which ranged from a five per cent reduction, from 2000 levels, by 2020 to a 25 per cent reduction in CO₂ emissions, from 2000 levels, by 2020, each of those scenarios had reduced GNP per capital growth by 0.1 per cent per annum. Obviously, there is rounding involved there but that is the order of magnitude of the cost.

Senator BOSWELL—For the uninitiated can you explain that to me. If you want to reduce your carbon footprint by five per cent it costs how much? Your modelling was five per cent.

Dr Gruen—We did four scenarios, if I am right—

Mr R Ewing—Yes.

Dr Gruen—of a range of cuts. We are always talking about them relative to 2000 levels. So these are not five per cent cuts compared to what would otherwise be the case; they are much bigger than that. A five per cent cut by 2020 relative to 2000 levels is a much more substantial cut from the level of CO₂ emissions than you would see if you did nothing. So these are substantial cuts.

Senator BOSWELL—I am taking it that this \$463 billion figure would be taken from 2020.

Dr Gruen—Indeed. The scenarios that we looked at had those sorts of cuts by 2020 and then they had very much bigger cuts by 2020 so you are on a path to an economy with very much lower levels of CO₂ emissions than are currently being emitted into the atmosphere. The estimates were as for each of those scenarios, and obviously they have different costs: the deeper the cuts the larger the costs. But they all round to about a reduction in growth of GNP per capita of 0.1 per cent per annum.

Senator BOSWELL—So if we were to cut our carbon emissions by 50 per cent by 2030 it would cut the growth by 0.01 per cent. Is that what you are saying?

Dr Gruen—It is 0.1. As Mr Ewing said, we did not do that particular scenario. But the scenario we did do, which was the Garnaut minus 25 scenario, has cuts which are not quite as deep as the ones you are talking about—we do not know exactly because we have not looked—but comparable.

Senator BOSWELL—So what was the outcome of that?

Dr Gruen—We did not report the results to two significant figures but to one figure it was a 0.1 per cent per annum cost to GNP per capita growth.

Senator BOSWELL—So if we go out and spend \$463 million by the year 2030 we are going to cut our GNP growth by 0.1 per cent.

Dr Gruen—Per annum. Except that I know nothing about the \$463 billion.

Senator BOSWELL—Well, that is the guts of the question. The ACTU want to put \$463 billion into decarbonising Australia by 2030. Your answer to me, and you may correct it, is that if we do that we are going to affect the GNP by 0.1 per cent.

Dr Gruen—No. I said the modelling that we did—

Senator BOSWELL—Can you just tell me what will happen if we—

Dr Gruen—I cannot tell you because I do not know the details of this report.

Senator BOSWELL—Maybe Mr Ewing has got the report there.

Dr Gruen—Even if he has, the point is we are not going to give you off the top of our heads, from what some detailed alternative modelling suggests, what our estimate is of the

economic cost of some alternative scenarios. We have done a series of scenarios which we have published and given extensive detail on. We can take on notice a question about what Treasury's estimate is of the economic cost of someone else's proposal but we cannot give you an answer here and now. Not even Mr Ewing can do that.

Senator BOSWELL—Well, if you would do that for me and if you would also put this on record now. You said you had modelled four scenarios. Can you tell us the four scenarios that you have modelled and the results?

Dr Gruen—This is all published.

Senator BOSWELL—I know, but I am asking you—

Mr R Ewing—I am happy to quickly recap the scenarios. We modelled two scenarios which were labelled the CPRS scenarios. The first, CPRS minus five, had a five per cent reduction of emissions against the 2000 benchmark by 2020 and a 60 per cent reduction by 2050. The CPRS 15 scenario had a 15 per cent reduction in 2020 and a 60 per cent reduction in 2050. Then there were two Garnaut scenarios. There was the Garnaut minus 10 scenario, which had a reduction of around 10 per cent by 2020, I think, going up to something around 70 per cent by 2050. But it was based on a per capita allocation, so it was a different approach. Finally the Garnaut minus 25 would have a reduction of 25 per cent in 2020 and a reduction of about 90 per cent by 2050.

Senator BOSWELL—Have you got the costs that are involved in that?

Dr Gruen—Yes. The cost for each of these scenarios rounded to one decimal point was 0.1 per cent per annum.

Senator BOSWELL—I do not know if this is the appropriate committee in which to ask this. How much overseas aid was given for climate aid? How much money was spent for overseas climate aid?

Mr Flanagan—Part of it is a definitional issue as to which parts would be ODA eligible. I would have to quickly go through and see which parts would be ODA eligible components, but that would probably be more a question for AusAID rather than for ourselves.

Senator BOSWELL—But you must know. You are the Treasury, so you must know.

Senator Sherry—Not necessarily. This is the macro area of Treasury.

Senator BOSWELL—Well, this is a macro question.

Senator Sherry—Whilst they have got massive and significant expertise, it is just a touch unfair to expect them to be able to lay their hands on other areas of estimates in detail quickly.

Senator BOSWELL—Okay. Maybe I could put it on notice.

Senator Sherry—Yes, we will take it on notice.

Senator BOSWELL—I have got a couple more questions. At the last estimates Mr Ewing told us that the Copenhagen outcome was broadly consistent with the assumptions used in Treasury modelling of the CPRS. I asked Mr Ewing why Treasury had not modelled the scenario of Australia going alone when the rest of the world did not have an ETS. Mr Ewing replied it was 'because it does not seem to me a very relevant scenario to be modelling. We

are not in a world where Australia is going to be alone. It does not seem that it is very relevant to model that.' In answer to my question on notice, Treasury replied just last week:

The proposals eventuating from the United Nations Framework Convention on Climate Change conference in Copenhagen last year are broadly consistent with the ... multi-stage approach ...

Has Treasury revised its earlier position and undertaken additional modelling of the CPRS perhaps involving different assumptions about international action post Copenhagen?

Mr R Ewing—We have not done any additional modelling as to what different international scenarios would look like at this stage.

Senator BOSWELL—On 27 April the Prime Minister cited slow progress in the realisation of global action on climate change as a reason for delaying the CPRS. He said international action had been slower than was originally anticipated and what 'we need is to make a judgment of what happens post 2012 and of what the rest of the world is doing' because the rest of the world and what they do was pretty important in terms of the Australian future. Isn't the Prime Minister's statement at odds with what you told us in February, that the international response was broadly consistent with Treasury modelling?

Mr R Ewing—I do not believe so because I do not believe the Prime Minister was referring to Treasury modelling assumptions in his statement.

Senator BOSWELL—He was not. You were saying the rest of the world was doing what Copenhagen did; it was consistent. He was saying it was not consistent.

Dr Gruen—We are not really in a position to make reflections on this other than to refer to the modelling we already did.

Senator BOSWELL—The government website says:

The Prime Minister announced that the Government will not introduce the CPRS until after the end of the current commitment period of the Kyoto Protocol (which ends in 2012) and only when there is greater clarity on the actions of other major economies including the US, China and India.

I was raising concerns that the Treasury has not modelled any action by other countries like China and India on ETS. You said that was not relevant, and the modelling will still work post Copenhagen. Yet now the Prime Minister says that we have to wait for global action before we can continue with the CPRS.

Were the Treasury outcomes wrong? You are inconsistent with what the Prime Minister was saying.

Senator Sherry—No, they are both right: Treasury is right and the Prime Minister is right. It is as simple as that.

Senator BOSWELL—So the world is going to go ahead and do what Copenhagen wants it to do, and the Prime Minister says it is not—everyone has got to advance—so you are both right. They are two things going totally 180 degrees the other way.

Senator Sherry—I think, firstly, as Treasury indicated, that you cannot go to them about announcements by the Prime Minister. Secondly, it is not the only reason, as you well know, that the Prime Minister gave. The Prime Minister also publicly referred to the failure of the

Senate to pass it—I could go into that in some detail; I will not—but that was also another reason given. If we cannot get the thing through the parliament it is just a bit tough.

Senator BOSWELL—That should not make any difference if you—

CHAIR—I think that Senator Eggleston has the call.

Senator EGGLESTON—I would like to ask a couple of questions with respect to the value of the Australian dollar. Our currency has depreciated significantly since the budget was handed down. Would a lower value of the Australian dollar be expected to change inflation forecasts?

Mr Gruen—It would depend on whether it were sustained. If it were sustained, it would have implications for outcomes, not only for inflation but for other things. But, of course, the Australian dollar is not the only thing that has changed; other things have changed as well, which is always the case. It is always the case that conditions evolve and circumstances change. I am afraid that is the situation that we find ourselves in often.

Senator EGGLESTON—Your inflation forecasts now incorporate assumptions about the future path of monetary policy in response to expected inflation, so what is your view of where interest rates will go? Do you think that they will be higher than anticipated by the Reserve Bank?

Mr Gruen—I do not speculate on future interest rate movements. It is certainly the case that the markets have changed their view of the future path of interest rates. At the time that the budget forecasts were being put together, the markets' expectations were that there were going to be further rises priced into the forward curve out to the end of 2009, and it is now the case, based on the latest information that I have seen, that the markets are not expecting any change in interest rates out to the end of 2009. The market has changed its view on the likely future path of interest rates.

Senator EGGLESTON—It is very interesting; so you are expecting—

Mr Gruen—Sorry—I said 2009; I should have said 2010. I apologise.

Senator EGGLESTON—I assumed you meant that.

Mr Gruen—It is important for me to keep in mind which year we are in.

Senator EGGLESTON—It is always a very good thing to do! You are suggesting, in fact, that interest rates will not change over the next few months?

Mr Gruen—I am not suggesting that; the market is. I am not making any comment.

Senator EGGLESTON—All right; that is a market assumption.

Mr Gruen—That is what the market is pricing in at the moment.

Senator EGGLESTON—I presume that is, in effect, an assumption by the market?

Mr Gruen—It is the outcome of people trading; different people have different views, but the weighted average of the money that is being put into the market is of that view.

Senator EGGLESTON—I think we are talking about the same thing.

Dr Gruen—I think we are.

Senator EGGLESTON—That is very interesting nevertheless. The Australian dollar has depreciated by over 10 per cent in the last few weeks, although other currencies of resource-rich countries have also fallen. The Australian dollar has in fact fallen by about double the rate of these other currencies with respect to the United States dollar. In your view, what are factors impacting on the fall of the Australian dollar in this way?

Dr Gruen—I think I might have answered this question while you were out of the room, Senator.

Senator EGGLESTON—My apologies.

Dr Gruen—That is all right. It is the case that since the end of April the Australian dollar has fallen by more than some other commodity exporting currencies, but I made the point in my earlier remarks that this was also a feature of what happened in late 2008 when the Australian dollar fell—certainly more than the Canadian dollar. When there is a rise in risk aversion in the world, which there currently is, one of the effects of that is that commodity prices come down and the other is that the Australian dollar tends to fall by more than other commodity currencies. It is particularly highly traded, and so people unwind long positions in the Australian dollar and that leads to larger fall.

What we have seen over the last month is broadly in line with what we saw in late 2008 in response to a rise in risk aversion in the world, although the scale of what we have seen over the last month is significantly less than the scale of what was seen in late 2008.

Senator EGGLESTON—That is very interesting, especially considering that other countries like South Africa and Canada are both resource-rich countries.

Dr Gruen—But as I said, if you look in 2008, you will find that at the time the Australian dollar fell a long way, as you would remember, and the Canadian dollar fell by significantly less than ours did at that time.

Senator EGGLESTON—Yesterday KPMG released a report entitled *Potential financial impacts of the Resource Super Profits Tax on new mining projects in Australia*. I just wonder if I could ask you some questions about this. This report shows large falls in the net present value of most mining projects in Australia and they, for example, say that there has been a 46 per cent fall in the net present value on financial models for iron ore projects; a 57 per cent fall in net present value on model black coal projects; a 15 per cent fall in bauxite projects; and negative net present values for nickel, copper and goldmines such that they may become economically unviable. If a company suffers a reduction in its net present value of its existing and future projects, what will happen to the share prices of those companies, do you think?

Dr Gruen—I am really not in a position to comment in any detail about a report that I have not seen, but obviously if a net present value of a company fell you would imagine that its share price would fall.

Senator EGGLESTON—Yes, that is a fair conclusion; I would think that as well. The report further concludes that the mining sector would not be able to source 40 per cent of its funding at the long-term bond rate. I ask: what would be the implications for mining investment if under the RSPT the mining sector cannot access finance at the long-term bond rate?

Dr Gruen—Since that exact issue amongst others goes to the implantation of the RSPT, I do not think it is helpful for me to speculate about that because it and the other design features of this proposed tax are the subject of the consultations that are currently going on between the Treasury and mining companies. I am certainly not the person to comment on this. The people you need to talk to about this are the people who are doing those consultations.

Senator EGGLESTON—Very well. Did Treasury conduct any analysis on the effect of the present values of different types of mining projects following the application of the RSPT?

Dr Gruen—Again, you really need to talk to the people who have been involved in this work rather than me.

Senator EGGLESTON—So we are not sure if the analysis was done, but we are assuming it may have been. Is that a fair comment?

Dr Gruen—I cannot comment either way. It certainly was not done by the macroeconomic group.

Senator EGGLESTON—I see. I will conclude there if you cannot answer further questions.

Senator BUSHBY—I have a few questions about the structural budget balance. In last year's budget you produced estimates of the structural budget balance, estimated at below negative four per cent, using certain assumptions about unemployment and terms of trade. I am referring in particular to the 2009-10 Budget Paper No. 1 at page 4-17. How would a decrease in the expected unemployment rate affect the structural budget balance if the underlying cash balance remained unchanged?

Dr Gruen—It would depend on whether you regarded the change in the unemployment rate as a structural change or a cyclical change. It would depend on that. If it were a cyclical change, you would get a different answer than if you thought that the decline in the unemployment rate was structural.

Senator BUSHBY—If it were structural, would it increase or decrease the structural budget balance?

Dr Gruen—Hang on, this is getting tricky. So the underlying cash balance has not changed and you want to know what would happen to the structural balance if you thought the structural rate of unemployment was lower; is that the question?

Senator BUSHBY—Yes.

Dr Gruen—I will do my best. The structural budget balance would be improved if the structural rate of unemployment fell, but if the actual underlying cash balance had not moved that would be a structural deterioration, assuming that the structural rate of unemployment was now lower. I think that is right.

Senator BUSHBY—I think that is what I needed.

Dr Gruen—I should add that we do not think there has been a structural decline in the unemployment rate.

Senator BUSHBY—You said it might well be different if there had been a cyclical decrease in the unemployment rate.

Mr T McDonald—Because the structural budget balance is based on a series of structural assumptions. If you take the position that the structural rate of unemployment is unchanged then if the actual unemployment rate is lower then any movements in the budget balance as a result of that would be assumed to be cyclical. So a reduction in the unemployment rate would be expected to result in an improvement in the underlying cash balance both through higher revenues and lower outlays. Then if the observed result was that the actual budget balance did not change despite the cyclical improvement in the unemployment rate then you would assume that the structural budget balance would have deteriorated.

Senator BUSHBY—That is what I expected. How would an increase in the expected terms of trade affect the structural budget balance if the underlying cash balance remained unchanged—would it increase or decrease the structural budget balance?

Mr T McDonald—This is perhaps even a trickier question than the one on the unemployment rate. What is quite difficult with things like the terms of trade is knowing exactly whether an improvement is because of cyclical factors or structural. Indeed, there are going to be cases where you get a little bit of both. If you were to assume that all of an increase in the terms of trade was cyclical in those circumstances then you would expect that increase in the terms of trade to result in a higher level of revenue and, therefore, an improvement in the underlying cash balance. If the result was in fact no improvement in the underlying cash balance that would imply a deterioration in the structural budget balance.

Senator BUSHBY—Has Treasury done any further work to estimate the structural budget balance as it currently stands? It was in the papers last year but I do not know if it is this year.

Mr T McDonald—We have done some work since last year's budget to refine, extend and monitor structural budget balance measures. We have not done the calculation based on this year's budget numbers.

Senator BUSHBY—Why is that?

Mr T McDonald—As you will recall, in last year's budget papers the analysis of the structural budget balance did not occur in isolation but rather occurred as part of a broader assessment of fiscal sustainability. In the discussion you had with Dr Gruen earlier about the chart that is in this year's budget I think Dr Gruen noted that that was one piece of evidence. I think we see a structural budget balance measure as being one part of evidence in a broader assessment of fiscal sustainability.

One thing we tried to do in last year's budget papers was highlight just how dependent these measures are on the assumptions that are made, in particular, as you referred, to the terms of trade. In the budget papers last year we said:

Alternative assumptions around the equilibrium terms of trade—that is, assumptions around the extent to which movements are structural rather than cyclical—can result in significantly different structural budget balance estimates.

Despite that, one of the things I keep learning with the experience is that, no matter what you put in words, people pay far more attention to figures. Historically we have resisted

publishing structural budget estimates for the very reason that there is excessive focus on point estimates rather than taking—

Senator BUSHBY—You published it last year. As you note, people focus more on figures than they do on the words. It was to some extent used for political purposes last year. This year it is not published. I am curious why—not that I am suggesting that Treasury would be complicit in any political activities. Is there the potential for this year to show that it has got worse and it is not there because of the potential to be used for political purposes again?

Dr Gruen—I will not comment on that, but I will make the point that the IMF and the OECD publish structural budget balances. Certainly the OECD have been making the point for a while that for a country like Australia the level of the terms of trade—the standard way of doing structural budget balances is not to talk about issues to do with terms of trade but to cyclically adjust—

Senator BUSHBY—Australia is a little different in that respect.

Dr Gruen—Exactly. So the OECD had issued a working paper sometime ago making the point that for commodity exporting countries like Australia it becomes extremely important what assumptions you make about the structural level of the terms of trade because that has very substantial implications for your revenue estimates, as everyone around this table would be aware. We had been doing some of this work ourselves, but we thought there was heightened interest in this issue, partly because the OECD drew attention to it and partly because the terms of trade had moved so much. There was a long period of time when small movements in the terms of trade were regarded as the norm, but obviously in the past six years or so the terms of trade have changed by an amount that we have not seen since the Korean War.

The issue of the implications of a very different structural assumption for the terms of trade were front and centre. We did some work in the budget last year and we published that work. But, as Mr McDonald says—and perhaps we should have been clearer—these assumptions are extremely sensitive to the detailed assumptions you make for the structural level of the terms of trade, and we would still make that claim.

Senator BUSHBY—In estimating last year's structural deficit, what value did you use for the terms of trade? What did you assume was the natural level?

Mr T McDonald—The value for the terms of trade was the same as the end point of the medium-term fiscal projections. The easiest way to look at this is to refer to the *Intergenerational report*, because it is equivalent to where the terms of trade finishes in the *Intergenerational report* projections.

Senator BUSHBY—Does it have a figure?

Mr T McDonald—It does have a figure. One of the slight complications is that the terms of trade figures from year to year are comparable but need to be adjusted because the ABS rebases the national accounts to a different year because it is an indexed number.

Senator BUSHBY—You would have had to assume a figure as the normal terms of trade to do a structural deficit calculation.

Dr Gruen—We could take it on notice and give you an answer.

Senator BUSHBY—I do not know whether you can tell me this: is the terms of trade now higher or lower than last year's assumption?

Mr T McDonald—It is higher.

Senator BUSHBY—If you take that other question on notice it would be very good.

Dr Gruen—The question you would like the answer to is what the level was assumed to be here and what it is now in the comparable period.

Senator BUSHBY—And also what you would consider the normal level is now, yes. You are saying it would be adjusted. With structural deficit calculations you assume capacity and normally that is your growth and your unemployment rate, but in Australia, because it is a commodity country, we also do terms of trade. I want to know what the assumption is for the purpose of last year and whether that has changed.

Dr Gruen—Yes, indeed.

Mr T McDonald—I guess on the first part of that, what we said in last year's budget was that the terms of trade assumption that we used was consistent with the end point of the medium-term projections outlined in appendix B of statement 3, and that says that the phase-down assumes the terms of trade decline by around 15 per cent from the end of the medium-term projection periods by 2022-23. That end point, when we reach it, is later now. But that end point is consistent with the equivalent end point in the *Intergenerational report* for the terms of trade. I believe there is a chart that has that. We can take it on notice to see what extra we can provide.

Senator BUSHBY—I have a couple of final questions on this. You mention you had done some work on the structural budget deficit this year. Would the structural budget balance be above or below the actual underlying cash balance for 2009-10 and 2010-11—that is, is the structural element of the budget expansionary or contractionary?

Dr Gruen—We may need to take that on notice because it will depend on the assumption you make, particularly for the terms of trade. Obviously the unemployment rate is much closer to our assumed full employment rate than we had thought it would be. We would have to take it on notice.

Senator BUSHBY—Are you aware of whether any other organisations produce structural deficit estimates for Australia?

Dr Gruen—I think the OECD does.

Mr T McDonald—The OECD and IMF do and Access Economics also does. Just one thing on the Access Economics estimates, I think they are in the *Budget monitor*. One of the things that the most recent *Budget monitor* has done is make a significant adjustment to the assumption that they make for the underlying or structural terms of trade estimate—quite substantially, as far as I can understand. That has an impact on their estimates as well.

Senator BUSHBY—Bearing in mind that impact, what do those other organisations say has happened to Australia's structural deficit over the last year?

Mr McDonald—Again there are questions of timing on this. I do not have the latest OECD ones because they have only just come out last week. The IMF estimate—

Senator BUSHBY—Can you take it on notice to provide the latest ones that came out last week?

Mr McDonald—Yes. The most recent ones from the IMF, which predate the budget and so are not necessarily directly comparable, are moving from in 2008 -0.6, 2009 -0.4, 2010 -4.9 and 2011 -3.5. That is covering all levels of government, state and federal and acts as a percentage of potential GDP, I think. Access Economics estimates—these are in financial years, starting in 2008-09—are -2.3, 2009-10 -3, 2010-11 -2.3, 2011-12 -0.8 and 2012-13 -0.6. I guess the point to note there, though, is that a key element, as you are saying before, of a structural balance budget estimate is what your estimate of the underlying cash balance is. Access Economics, and again this budget monitor predated the budget, including the savings features in the budget, had an actual underlying cash balance of -0.5.

Mr Gruen—In 2012-13.

Mr McDonald—In 2012-13, which is only slightly different to the structural budget.

Senator BUSHBY—I will have a look at those figures and think about those later. I am not sufficiently au fait with it all to actually analyse all that and get into it. So we will move on to something else.

CHAIR—Senator Cameron has a few questions.

Senator CAMERON—Mr Ewing, I think I have asked you previously about a Minerals Council report entitled *The Employment Effects on the Australian Minerals Industry from the Proposed Carbon Pollution Reduction Scheme in Australia*. That was a Minerals Council Concept Economics report of 21 May 2009. You are aware of that report?

Mr Ewing—I am aware of that report.

Senator CAMERON—I note that the Minerals Council has this morning produced a KPMG report. You are aware of that?

Mr Ewing—I have heard reference to it, but as I have been here since 9 am I have not seen anything on it.

Senator CAMERON—So now we have got two Minerals Council reports out in the public arena. I want to take you back to the original report, the May 2009 report. Are you aware that that Concept Economics report said that there would be 23,510 less jobs in regional Australia than otherwise would be the case as a result of the government's proposed CPRS?

Mr Ewing—That sounds like the estimate from the report and I do not have it in front of me.

Senator CAMERON—Are you aware that the Minerals Council then put out a press release claiming that there would be 22,510 less jobs, yet what they neglected to say was 'than would otherwise be the case', that in fact on the Minerals Council's own website a National Institute of Labour Studies report had said that over the period there would be a growth of 86,000 job. So really, instead of the position being that 23,510 jobs would be lost, there would be a net growth of 62,490 jobs in the mining industry?

Mr Ewing—That sounds correct, although I should caution that you should be careful when adding together employment numbers from two disparate studies because that can lead to misleading results. But I believe that that is a relatively accurate summary, from my knowledge of those reports.

Senator CAMERON—I am worried about the Minerals Council coming out with these reports and then misrepresenting them. This Concept Economics report has some flaws, from your analysis, like unspecified reference scenarios, ignoring dynamic responses and changing prices and circumstances in regions. Is that correct?

Mr Ewing—Yes, that is correct.

Senator CAMERON—Can you outline some of the flaws in that report?

Mr Ewing—I believe we provided an answer to that on notice previously. There are several issues to be noted in that report. In particular there is an ‘off-model adjustment to the mining and smelting industries’—no details are provided on that adjustment or how they are important for the results. There is no aggregate whole economy impact reported, which makes it very hard to compare this work or get a sense of how its overall macroeconomic impacts fit into the general picture of the very substantial range of reports that have been released. In the absence of that context, it can be quite difficult to judge some of the detailed results of the report. The analysis is reported entirely in terms of output and employment changes relative to an unspecified reference scenario. That means that, while it mentions ‘23,500 fewer jobs than would otherwise be the case’, no information is provided as to what ‘would otherwise be the case’. That makes it very hard to judge the materiality of these impacts. It also makes it difficult to judge the economic circumstances which the consultants have used in their overall report. I believe those are the major issues.

Senator CAMERON—So, back in May, if the Minerals Council was prepared to go out and argue that 23,500 jobs would be lost, that is a misrepresentation of even the Concept Economics report?

Mr Ewing—I would certainly say that the description ‘23,500 jobs lost’ was an inaccurate description of the concept modelling.

Senator CAMERON—The Concept Economics report was inconsistent with the modelling that was done for the CPRS by Treasury and others?

Mr Ewing—It is a bit hard to judge exactly how inconsistent it was, because there were not full details on important questions such as the reference scenario and the overall economic impact. I really cannot answer for certain how consistent or otherwise it was. They simply did not provide enough information.

Senator CAMERON—I suppose, given the misrepresentation that the Minerals Council and its chief executive, Mitch Hooke, put forward in relation to that first report, we will need to be very careful of misrepresentations from the Minerals Council and the KPMG report. Sorry, I will retract that.

CHAIR—Senator Bushby now has some questions.

Senator BUSHBY—I refer to comments made by Dr Henry at the additional estimates hearings in February on the passing of the financial crisis:

What people have called the global financial crisis, that has passed, I think it is safe to say, but that is not to say that there will not be further adverse shocks for financial markets down the track. ... I do not imagine shocks of the sort that would be globally significant, ...

Do you stand by Dr Henry's comments in that regard? Is that still the situation, given the events that have transpired?

Dr Gruen—There have been further shocks, as Dr Henry alluded to. Whether they will be of global significance is yet to be seen. There is certainly substantial significance to Europe. The shocks that are coming from the periphery of countries in Europe which are the most affected are serious developments which I think have profound implications for Europe. It does remain to be seen how big the implications are for the rest of the world. I say that because, although we have seen signs of tensions, if you like, in financial markets, at least thus far, those things have been much more contained. They are nothing like the order of magnitude of the post Lehman Brothers period or even of the period before then. In other words, the spreads have gone up but they are still quite low by the standards even of the period from the middle of 2007 to September 2008.

Senator BUSHBY—The context is set very well for my next question: what are your views on the comments made by the governor of the Bank of England on 12 May 2010? He said:

... the financial crisis is far from over. As debt has moved from the financial to the public sector, the banking crisis has turned into a potential sovereign debt crisis.

And, further:

America, and many other large economies including the UK, share some of the same problems as Greece with its public finances ...

It is absolutely vital, absolutely vital, for governments to get on top of this problem. We cannot afford to allow concerns about sovereign debt to spread into a wider crisis dealing with sovereign debt. Dealing with a banking crisis was bad enough. This would be worse.

Those are quite alarming statements, particularly coming from the governor of the Bank of England.

Dr Gruen—Yes.

Senator BUSHBY—You mentioned the potentially serious consequences for Europe and certainly I would understand that Australia's debt is nowhere near as severe and as concerning as the countries that were mentioned by the Bank of England governor. Nonetheless, the banking crisis—the subprime mortgage crisis—was not a crisis in Australia but had the potential to affect Australia.

Dr Gruen—Yes.

Senator BUSHBY—Similarly, if there is a sovereign debt crisis that does impact with the severity that the Bank of England governor is concerned about, that has the potential to impact in a big way in Australia.

Dr Gruen—I make a couple of points. Thus far it is the case that the countries that have been very severely affected have two characteristics. One is that they have either high or very high levels of government debt and they have large budget deficits. That is the first

characteristic. The second characteristic is that they are in the euro area so they do not have control over their own monetary policy or their own exchange rates, and they have become very uncompetitive. All the countries that we are talking about—Greece, Portugal, Spain, Ireland and in principle you could perhaps add some more, but let us start with them—are all part of the euro area and they all have their price levels well out of line with the core countries of the euro area. Why is that important? It is extremely important because it means that fiscal consolidation in those countries cannot be offset by a depreciation of a currency or an easing of monetary policy, because they simply do not have those instruments. Why is that important? Because fiscal consolidation in those countries will substantially hurt growth in those countries and the fact that growth is hurt means that the fiscal problem looks even more diabolical, because you are not growing or in fact you may even be contracting, so your GDP is not growing and you are trying to get this debt under control.

Senator BUSHBY—I understand the difficulty—

Dr Gruen—Let me go on. Thus far, a consequence of these developments in the periphery of the euro area has been that bond yields in a lot of other countries, including countries with quite high levels of government debt—namely, the UK, Japan, Germany; these countries have different levels of government debt—

Senator BUSHBY—Yes, but they have substantial levels.

Dr Gruen—I do not want to make the claim that they are all high. They are substantial; they are not all high. The bond yields in Germany, the UK, Japan, the US, and for that matter here, have fallen. So thus far the situation has been that there is no sign of contagion from those problems to countries which have control over their own currencies and monetary policy and are in the process of either engaging in fiscal consolidation themselves or they are projecting it in their futures. That is an important distinction, because I think the governor of the Bank of England is making the point—obviously his words go all around the world, but they have particular resonance for his own country—which is an extremely point to make, that you need to retain the confidence of financial markets and therefore you need to have a credible policy for fiscal consolidation.

I can absolutely understand why he makes that point. It is a point that I would make as well. So I guess my point is that the events in the periphery of Europe are very troubling for the euro area. Those countries are in very difficult circumstances but the rest of world is not suffering from contagion from that, at least not in bond yields. But it is definitely the case that fiscal consolidation will be necessary in all of the countries that have very significant budget deficits. That is something that needs to happen over the next several years.

Senator BUSHBY—And that includes the UK and others—particularly in the UK, given that is where he was talking about. I think some of those comments may well have been made in support of announcements by the new government in the UK to actually fiscally consolidate.

Dr Gruen—That is right. The balancing act that those countries have is particularly difficult because in the ones where growth is still fragile they suffer from the fact that if you do fiscal consolidation too rapidly you can turn the economy back into a recession—which is what happened in 1937 in the United States.

Senator BUSHBY—It is certainly a potential. But I think he is saying that the alternative may be worse.

Dr Gruen—Absolutely. You are in a difficult circumstance and there are serious trade offs about what you do.

Senator BUSHBY—We will move on from there. I have asked questions about this before, particularly to Dr Henry. Essentially, budget forecasts are only as good as the underlying economic assumptions and the recent performance in forecasting key economic parameters has not been good. For example, last year's budget forecasted that the Australian economy would contract by 0.5 per cent in 2009-10; this year's budget tells us the economy will grow by two per cent.

Dr Gruen—Yes.

Senator BUSHBY—Last year's budget said the unemployment rate would peak at 8.5 per cent in 2010-11; this year's budget tells us the unemployment rate has already peaked at less than six per cent and is headed to a low of 4.75 per cent in 2011-12. These very significant changes to the underlying forecasts over the space of just one year illustrate that there is a large degree of imprecision in the budget numbers. Is that a fair comment?

Dr Gruen—This last year was a particularly difficult one. There is no question that there is a margin of error around forecasts.

Senator BUSHBY—Did you know at the beginning of the year that it would be a particularly difficult one?

Dr Gruen—Yes.

Senator BUSHBY—How confidently can you actually state then, if you know it is going to be a difficult one, what the figures will be in the coming year?

Dr Gruen—We were in the midst of the worst synchronised global downturn since the Great Depression and having a sense of how that was going to turn out was a tricky thing to do. We, along with a lot of other people, underestimated how quickly the Australian economy would bounce back. There is no question of that. Our forecasts were actually quite close to consensus forecasts at the time but as events have turned out, the outcome has been stronger than any of the forecasters who contribute to the consensus forecasts—there are 17 of them—expected. The outcome has turned out to be significantly stronger than anyone expected.

Senator BUSHBY—Do you think that the coming year or the coming years will be difficult as well?

Dr Gruen—I am hoping that conditions are going to be more normal and therefore that forecasting will be less fraught than it was last year.

Senator BUSHBY—On the basis of what you know, though? You say you 'hope'. That is not—

Dr Gruen—I agree. I should take it further than 'hope'.

Senator BUSHBY—On the basis of what you do know about the current economic state of affairs worldwide, do you think that it will be a normal year or is it likely to be?

Dr Gruen—Not completely normal, for the reasons that we have just been discussing. But it is certainly the case that conditions in financial markets are much closer to normal than they were in April or May of last year.

Senator BUSHBY—So better than last year, but not fully normal?

Dr Gruen—Not completely normalised.

Senator BUSHBY—And that may well have an impact on the actual figures as they turn out?

Dr Gruen—It is possible, yes.

Senator BUSHBY—You mentioned that the outcomes were far better than anybody predicted, including your own figures. As it turned out and with the benefit of hindsight, do you consider that the size of the fiscal stimulus was required? Was that quantum actually necessary, given where it ended up?

Dr Gruen—I think the conclusion that I have actually said before is that I think the fiscal stimulus and, for that matter, the monetary stimulus was more effective than we thought it would be. There were other things that also helped.

Senator BUSHBY—Obviously, looking back you can analyse it—

Dr Gruen—Yes.

Senator BUSHBY—but there are two ways of looking at it: (1) it was more effective; or (2) it was larger than it needed to be. Is there any evidence that you can point to that would help us decide which one of those paths you would actually take on an informed basis?

Dr Gruen—Yes, but judgment about whether something is bigger than it needed to be is a judgment about whether you would be comfortable with a profile for unemployment that was higher than the one we have turned out. So it is a cost benefit analysis that involves a trade-off between allowing the unemployment rate to be higher for longer and expending less money.

Senator BUSHBY—It is in a general sense but—I am running out of time to do this.

CHAIR—I am afraid you are. We could continue on for a long time but I think we have stretched the patience of the macro officials and tested their knowledge long enough. Thank you for staying longer than was initially required.

Proceedings suspended from 1.00 pm to 2.01 pm

CHAIR—Welcome to the Treasury Fiscal Group. Mr Ray, do you wish to make an opening statement?

Mr Ray—No, thank you.

CHAIR—We will start with questions straightaway. Senator Bernardi.

Senator BERNARDI—Mr Ray, I want to specifically address the role of the Minister for Population and population policy. So if you can point me in the right direction.

Mr Ray—Mr Murray is looking after that area.

Mr R Murray—The new population minister was appointed by the Prime Minister. He has a specific task over the next 12 months to develop a population strategy. The aim of this

strategy is to look at various scenarios around population growth, taking into account various drivers of that, a lot of those being around economic and social issues, and then to look at the opportunities and challenges coming out of that. As the Prime Minister set out in his press release, some of those challenges are around economic development and a subset of that are around growth and development of Australian regions, towns and communities. Also, the aim of this strategy is to take into account not only the challenges but also the opportunities that exist around cities—planning, the urban amenity, transport infrastructure and those sorts of issues. Finally, to take into account clearly all of the environmental constraints around population and, in particular, issues such as water and also other issues related to climate change and the like. It is to look at a holistic approach. The minister is being supported by a task force in Treasury and we are approaching this task with a very right-across-government approach, a very collaborative approach. We are trying to ensure that we take into account every aspect of this subject in coming up with an overall population strategy.

Senator BERNARDI—When was Treasury advised that a Minister for Population would be commissioned?

Mr R Murray—The Prime Minister's announcement was on 3 April, and I think that was a Sunday.

Mr Ray—Yes, a Sunday.

Mr R Murray—There were some discussions around that prior to that date?

Senator BERNARDI—How far prior—the day before, a week before, a month before?

Mr R Murray—I am not too sure on that. There were various discussions amongst ministers but certainly, in the weeks leading up to that, there were various discussions. We certainly supplied some input, but there was input from various other sources.

Senator BERNARDI—And so you are unable to give me a specific date when Treasury were advised that a Minister for Population was going to be appointed?

Mr R Murray—We probably became aware of it literally a day or so before that.

Senator Sherry—We will take that on notice and get you the exact date. As to the conversations, briefings, advices to ministers and discussions prior to that, obviously that will not be provided.

Senator BERNARDI—Were you consulted in regard to the placement or the additional responsibilities for Treasury to handle the population policy portfolio prior to the announcement?

Mr R Murray—There were certainly some discussions between ministers and certainly with the Treasurer but, if we are given a task, we are given a task.

Senator BERNARDI—But the department was not consulted prior to the appointment being made?

Mr R Murray—No, I am not saying that. Certainly, discussions were held. We were certainly privy to at least some of those discussions. Ultimately, this is a matter for the Prime Minister to decide in terms of arrangements regarding government administration. So the final decision of course was with him and his cabinet colleagues.

Senator BERNARDI—When the announcement was made, were any additional resources allocated in the form of staffing to Treasury to undertake this task?

Mr R Murray—Our view on all of this was that, for the first few months of this, we could handle this within our own resources. We had already invested, as you know, over maybe seven or eight years significant resources in this whole area and those resources have been the backing for the intergenerational reporting process. So we have a certain amount of resources both within our budget policy area, a fiscal group, but also backed up in the revenue group, in the micromodelling area. So we already had a significant amount of resources that we knew we could immediately back this up with, but then in the budget we were allocated another \$1.25 million to cover the task force for the rest of its period, so through the fiscal year 2010-11.

Senator BERNARDI—How many additional staff for your task force will that \$1.3 million cover?

Mr R Murray—Out of our own resources, during 2010-11, we are budgeting out of our own base resources about \$800,000, which will account for about four or five staff. Depending on how you cut up the \$1.25 million, we have budgeted—and this is what is in the costing—for an extra six staff. So we are looking at a task force of about 10 or 11 people. We have some resources in there for administrative costs as well.

Senator BERNARDI—Given that your existing resources, though, were used to produce, among other things, the *Intergenerational report*, I would make the presumption—and please correct me if I am wrong—that they were adequately utilised in the previous six or seven years and they were not just sitting around twiddling their thumbs?

Mr R Murray—We use all our resources pretty flexibly. I do not think there is anyone down at Treasury twiddling their thumbs.

Senator BERNARDI—No, and that is the presumption I make.

Mr R Murray—I beg your pardon?

Senator BERNARDI—That is the presumption that I make. So what area of Treasury will then be neglected, because these people are going to be tasked in a new task force?

Mr R Murray—It is a matter of priority and a matter of how much effort you put into various areas. In terms of the modelling side of this, a lot of this modelling goes on anyhow and it is not just related to issues like the IGR or population. A lot of modelling goes on around distributional issues, retirement incomes et cetera. So that area works on various tasks, including population. That is the first point.

We can also use the four resources that we ourselves put into the task force quite flexibly, back into the budget process. So we have ensured that within the fiscal group, which Mr Ray heads, that, if needs be, we can use these resources pretty flexibly. But, for the next 12 months, their main task will be the population strategy.

Senator BERNARDI—In the last two months, can you inform me what the task force has been doing?

Mr R Murray—We have been going through a significant data process, and a significant process of pulling together a whole lot of policy information. Bear in mind that we have been significantly preoccupied with the budget and budget processes at the same time. What have we been doing? We have been looking at a whole lot of areas where we do not have primary carriage. We have been trying to bolster our knowledge base on immigration for instance and we have started looking, in particular, at regional aspects of a lot of the issues that are coming up.

In the Treasury we also now have responsibility over housing supply and the COAG processes that are trying to improve housing supply. So again we have been trying to bolster our knowledge base in that area—for COAG and also to help with the population strategy. Related to that, we have been trying to bolster our recourses around cities and infrastructure. So we have been doing a lot of this pre-work. We are putting together the building blocks of this whole exercise. In addition to that we have been briefing the minister. So as we get up to speed; he is getting up to speed as well.

Senator BERNARDI—Could you tell me what policy levers are available to government in regard to population policy, according to your research.

Mr R Murray—It all depends how you define population policy. There are various levers over population itself, and there are various levers about how you might deal with an ageing population or a growing population or whatever. In terms of population itself, obviously there is little that you can do around fertility rates and mortality rates—which are the main drivers of the natural increase in population. There have been significant movements in both those areas but a lot of that is beyond the control of governments. So the main lever for a country like Australia is around migration levels.

Senator BERNARDI—It does not surprise me. I think that is a commonsense approach except the minister said that growth is not only—or principally—driven by immigration figures. He wants to find how creative he can be in terms of the policy levers that we have available to us. I will give you the full quote. He said:

... the growth there isn't only driven by immigration figures, it's also driven by an increasing birth rate and it's also significantly driven by people moving there from other parts of Australia. So I want to find out just how creative we can be in terms of the policy levers that we have available to us.

You have just said that you cannot do much about the birth and death rates, really.

Mr R Murray—Certainly, I do not think I need to comment on death rates.

Senator Sherry—With death rates, we can lower smoking, for example—

Senator BERNARDI—We are doing our best, Senator Sherry.

Senator Sherry—I think we could be a bit more—

Senator BERNARDI—The net natural growth rate is how I should describe it.

Senator BUSHBY—I think the death rate works out at 100 per cent!

Senator SHERRY—Okay, let's leave that one and get back to birth rates.

Mr R Murray—Certainly, successive governments have made advances in that area in terms of overall public policy and there have been significant advances in technology so there

is an ongoing increase in life expectancy. Mr Gallagher could give you the details on that. On the overall fertility rates, the issues that appear to be major drivers for developed countries such as Australia are around income for women and education levels of women. In addition to that, where governments can play a part, significant studies by the OECD indicate that family friendly policies—particularly workplace policies and employment policies with respect to childcare—can have an effect.

For instance, where those policies are quite positive—that is, in countries like Australia but particularly in northern Europe—you do have high participation by women in work and also higher fertility rates. It sounds counterintuitive, but women, even though they are on a higher income and have higher education levels, do have higher fertility rates if they feel that they have a positive outcome in their work environment and their child care. So there are some levers there that you could pull but they take a while to come into effect and they, in some ways, are related to how you might change the culture and the outlook around those issues.

Senator BERNARDI—In your modelling for the *Intergenerational report* you would take some of those issues into account, surely? Mr Gallagher, I see you nodding, so this question will go to you I guess. You forecast not changes in policy settings but improvements in health care and a change in fertility rates; is that correct?

Mr Gallagher—For fertility we look at the trends in age-specific fertility rates and we project each age group on the basis of its trend and that trend continuing. So the big change that we are seeing in Australia is that women under the age of 30 have had declining fertility and women over the age of 30 and women over the age of 35 have had significant rises in fertility. This is associated with women deferring both marriage and childbirth until they are more economically established. The fertility rates, as Richard has been explaining, seem to be most responsive to the opportunity cost of having children. So in societies such as that of Italy, where married women are supposed to leave the labour force, women defer getting married and having children for a very long time. The result is that Italy has a total fertility rate of 1.2 compared to that of Australia, which is running at 1.9.

Senator BERNARDI—To continue along that line: if Australia has a net natural growth rate, which is net births—less the deaths—and no immigration, the forecast in the *Intergenerational report* I think was 26 million; is that correct?

Mr Gallagher—Yes: 26 or 25.5.

Senator BERNARDI—It was around that mark?

Mr Gallagher—Yes.

Senator BERNARDI—So the balance of the *Intergenerational report* forecast of an increase in population was—

Mr Gallagher—Yes, but of course migration itself contributes to fertility and will eventually contribute to deaths as well. It will change the natural increase numbers; it is not separate.

Senator BERNARDI—Yes, but in the *Intergenerational report* 36 million was the forecast.

Mr Gallagher—Yes, so—

Senator BERNARDI—So the figure, in round terms, is 26 million, or 25½ million, if we have no further migration. The balance of it is migration?

Mr Gallagher—Yes.

Senator BERNARDI—So that migration is a key, substantial driver of Australia's future population growth is a reasonable position to take?

Mr Gallagher—Yes: a substantial driver of our current population growth.

Senator BERNARDI—Do you have to hand the migration figures from last year?

Mr Gallagher—Yes, I do. The last publication we had from the Australian Bureau of Statistics came out on 25 March 2010. It has the Australian demographic statistics. Page 11 of the report gives both the annual migration numbers and the financial year migration numbers, as well as quarterly results.

Senator BERNARDI—Could you give me the figure. I do not have it in front of me.

Mr Gallagher—For 2008-09 net migration was 298, 924 and for calendar year 2008 it was 301,196.

Senator BERNARDI—The figures in the *Intergenerational report* assume an immigration intake of significantly less than that; is that correct?

Mr Gallagher—That is correct.

Senator BERNARDI—If you extrapolated these figures from, say, 300,000 over the next year for the next 40 years, which is the business as usual case, our population would be quite a bit higher than 36 million.

Mr Gallagher—Our population would be about 43.9 million.

Senator BERNARDI—43.9 million. So does that render the *Intergenerational report* kind of irrelevant, within the policy settings here?

Mr Gallagher—No. I think that we had probably six or seven reasons for thinking that migration would drop. Firstly, we knew that the Department of Immigration and Citizenship was doing policy reviews and that there would be a review of the skills in demand categories, the 457 categories and the student visa categories. We knew that, in terms of the high student intake of temporary residents, who stay here more than a year and therefore become part of the resident population, there had been a significant number of closures of vocational education and training institutions. We knew when we did the report—remember, we set the assumption back at the end of 2009—there were issues about Indian students which meant that we suspected there would be a drop-off in Indian students. At the time the assumption was set, we also thought that Australia's economic growth would be affected significantly by the global financial crisis and that unemployment rates—if you remember the budget forecast of the time—would be significantly higher. It was also the case that the Australian dollar was high, which would make it more difficult for overseas students to come in. In looking at the assumption, we considered that factor, and that meant that there was likely to be a drop, and then we considered where that drop might go to. We realised that both the Australian Bureau of Statistics and the Department of Immigration and Citizenship were using assumptions at

the level of 180,000 in their own thinking about long-term net migration and so we settled on that level for the purposes of the *Intergenerational report*.

Senator BERNARDI—This is what I find interesting: you are making assumptions about changes to policy settings in the future, and yet the minister has said on a number of occasions that the *Intergenerational report* is based on a business as usual approach over the last 40 years. If we were going on business as usual, we would be on track for a 43.9 million population.

Mr Gallagher—It was also the case that if we had looked at the average for the last five or 10 years we would have arrived at a substantially lower net migration figure. If we had looked at the average for the previous five years, I think we would have come out with 180,000 anyway. So it was perfectly consistent. It is the normal thing when you are doing projections, which is that you do not project off the top of a cycle. You do not project off the peak. You assume some return to average levels for a long-term projection.

Senator BERNARDI—That would be assuming that there was a similar policy setting in place. There was a change in government, I am loath to remind you, Mr Gallagher, a couple of years ago!

Mr Gallagher—But the increases in net migration began occurring before the change in government. In 2005-06, on the ABS numbers, net migration was 146,750. In 2006-07, it had already risen to 232,824. Then in 2007-08—and the current government was not elected until November 2007, so it did not have much say in this—the number had already risen to 277,000. The rise was already on.

Senator BERNARDI—But you must have a figure for the average over the period of the previous government. The economic cycle was somewhat different to the one we have got now.

Senator Sherry—Before we go any further with the answer, that was off a figure in 1997-98, under the former government, of 79,200. So if you contrast the movement and in fact—

Senator BERNARDI—That would have been in the guts of ‘the recession we had to have’; is that right?

Senator Sherry—Can I finish my answer.

Senator BERNARDI—You are trying to be misleading.

Senator Sherry—I am entitled to contribute to answers, if I want, without being cut. In fact, I can give you all the figures from 1996-97 through to 2007-08. There is significant long-term growth, and the figures are significantly different from year to year; hence Minister Burke’s reference, which you referred to earlier, about the long-term historical average. You asked for an average, for example, over the last 40 years. I am sure we can—

Senator BERNARDI—No, I did not.

Senator Sherry—If we do not have the figure here now I am sure we can calculate it for you.

Senator Bernardi—I did not ask for an average over the last 40 years; I asked for an average over the life of the previous government.

Senator Sherry—I am sure we can give that to you as well. I am happy to take that on notice if we do not have an average figure here now.

Mr Gallagher—The other rationale for the number is given on page 8 of the *Intergenerational report*. It shows a graph of what is called the rate of absorption of net overseas migration. That graph shows that the average level of net migration appearing to go back into the 1970s up until recently is about 0.6 per cent per annum. If you took that out, you would get an assumption which is consistent with what we have actually used. There are a variety of averages which supported the use of 180,000 as the net migration assumption, given that on any analysis of the data the number is highly variable.

Senator BERNARDI—The number of migrants?

Mr Gallagher—The number of migrants is highly variable.

Senator BERNARDI—It is highly variable. Has it in recent times, apart from the last financial year, exceeded 300,000?

Mr Gallagher—I suspect that 300,000 would have been a record. I do not know that we got quite that high in terms of post World War II migration. We would have been very high at that point, particularly in relation to population.

Senator BERNARDI—In summary, then, we have had 298,000 in 2008-09 and 301,000 this year.

Mr Gallagher—The 301,000 was for 2008. In 2008-09 it was 298,000. So there was a slight drop there.

Senator BERNARDI—It has averaged 300,000?

Mr Gallagher—Yes, basically.

CHAIR—Before we go too much further, I am assuming that we will finish with the population section by the afternoon tea break at three o'clock and then finish the rest. Is that everyone's understanding?

Senator BERNARDI—I am looking at Senator Brown, who probably has a few questions of his own. Would you be happy to divide the time, Senator Brown?

Senator BOB BROWN—Yes.

CHAIR—Do you want to go to Senator Brown and then take it up to three o'clock?

Senator BERNARDI—I am happy to, but I do have about another 10 minutes or so, or 15 minutes, if I can have them.

Senator BOB BROWN—Yes, I expect you will have that, at least.

Senator BERNARDI—Okay, then I am happy to cede to Senator Brown.

Senator BOB BROWN—Is economic growth predicated on population growth?

Mr Gallagher—The framework that we used for the *Intergenerational report* is often described as the three-P framework: productivity, participation and population. The total size of GDP is influenced by each of those factors and all combined.

Senator BOB BROWN—Is it possible to have economic growth without population growth?

Mr Gallagher—With increasing participation and increasing labour productivity it is possible to have economic growth, as is discussed. At the moment we have about 260,000 births on 130,000 deaths a year. You will get population growth from natural increase. It is very hard to stop population growth in Australia. As we have been discussing, the lever is overmigration.

Senator BOB BROWN—Yes, but I am really interested to hear from Treasury that it is possible to have economic growth without population growth. Could you tell the committee how that scenario may unfold?

Mr Gallagher—I think that, as we have already discussed, even if we went to zero net migration, we would end up with population growth to 25 or 26 million people. In that scenario there could be increasing labour force participation, which would contribute to economic growth. Certainly you would hope that there would be growth in labour productivity that would contribute.

Senator BOB BROWN—Ultimately we are in a finite world and we have to accept that population globally has to stop growing.

Senator Sherry—I think that is an opinion, Senator Brown.

Senator BOB BROWN—I am asking what your view on that is.

Senator Sherry—I do not accept that.

Senator BOB BROWN—You do not accept there is any limit to population growth?

Senator Sherry—It is an argument just as much as a question. I do not accept it and, if Minister Burke has anything more to add in detail, I will take it on notice for him to give you are response.

Senator BOB BROWN—Thank you. So you see infinite population growth as the reality that we have on the planet?

Senator Sherry—I did not say that. I said I do not agree with your view and the way you put your question. I am more than happy to take it on notice to get you some more detail from Minister Burke.

Senator BOB BROWN—With the projection of current immigration and population being in excess of 40 million by midcentury, what would the population of Sydney and Melbourne be under those circumstances?

Mr Gallagher—We have not done a regional analysis on the high projection growth. We have done a regional analysis which is consistent with the central projection in the intergenerational report. I have not brought that with me, but essentially we were looking at the major cities almost doubling in size. Given that we are at 22 million people now, to get to 35.9 million we are adding a considerable amount to the population and the history of regional growth in Australia is that most of the growth has been in the major cities on the coast.

Senator BOB BROWN—Has Treasury done an estimate of the cost of the infrastructure that would be required to facilitate, with increasing living standards, those populations in Sydney and Melbourne of about 7 million by midcentury?

Mr Gallagher—I have not. I do not know if anyone else has.

Mr Murray—We have not done that. That is not to say we are not going to do that. There is certainly analysis that can be done around the sorts of needs there might be for infrastructure. A lot of that would be at a fairly macro level, but there are some metrics that you could use that relate infrastructure back to what the stock of infrastructure that we have now is, what the growth of economic activity will be and what the relationship would be back to the need for infrastructure. A lot of that is quite difficult and relates to what the policy settings you might have around the supply of infrastructure are, for instance, around water. What are you going to do around the pricing of water? What are you going to do around the trading of water and trading between urban water and rural and industrial water? So a lot of that is fairly difficult, but it is possible. Like a lot of this modelling, it would take significant effort. Infrastructure Australia have been tasked with at least looking at the near to medium term in terms of certain areas of infrastructure needs and hopefully a lot of their analysis will shed some light on some of these questions.

Senator JOYCE—You have brought up water and we have before us the Wentworth report that talks about a 30 per cent reduction in water for the Murray-Darling Basin. So when these 22 million people turn up, what are they going to eat?

Mr Murray—I think people have to think pretty carefully about issues around food and food production. Trying to project forward what is going to happen to the industrial structure of Australia is pretty difficult. There will be a lot of market forces going on and a lot of factors will come into play.

Senator BOB BROWN—Just on that question, coming from what Senator Joyce asked, you are using current food production in Australia. Would that be adequate for a population of 36 million?

Mr Murray—I do not know. We are a significant exporter of food at present. What happens in the overall trade is an important issue, and what happens in the overall effects, say, on our terms of trade is again an important factor in terms of driving the economy.

Senator BOB BROWN—Could you take that—

Senator Sherry—We can take on notice—

Mr Murray—But also, Senator Brown, if we are looking at projected population figures, I think we would provide you with not just current net production figures in agriculture but net projected agricultural figures, because there will be productivity improvements and output improvements that may be identified. I do not know whether those figures are available but we will certainly supply them.

Senator BOB BROWN—Minister, have you taken into account the Garnaut report which estimates that on current climate change projections with business as usual, productivity in the Murray-Darling Basin may be reduced by over 90 per cent this century.

Senator JOYCE—Then you will be very hungry.

Senator BOB BROWN—Have you correlated that with the population growth that is being projected here?

Senator Sherry—What I have indicated here, Senator Brown, is that we will take on notice what you started to ask for and which I think I anticipated, which is the current net surplus agricultural production for Australia and also, if it is available and I do not know whether it is, the projected surplus of agricultural production in what I think is the relevant year here, which is 2050.

Senator BOB BROWN—Yes, whether the current food production would be enough for that population.

Senator Sherry—And also the projected food production is enough for the projected population.

Senator BOB BROWN—You may do that. I am not asking that question. I am asking the question about current—

Senator Sherry—I am always trying to be helpful so if we have got that figure I will provide that as well.

Senator BOB BROWN—And I will get it back to you as an answer to your question. Is Treasury tracking the rapidly diminishing food reserves of planet Earth in view of the growing population?

Mr Murray—Not that I am aware of.

Senator BOB BROWN—Would you—?

Mr Murray—Well, the answer is no.

Senator BOB BROWN—Would you have a look at that and come back to me with how Treasury assesses those figures—from the UN.

Mr Murray—We can certainly take that on notice.

Senator BOB BROWN—The UN report that is flagged in the *Guardian Weekly* and in a number of newspapers, with an article indeed in the *Hobart Mercury* this week, projects that loss of biodiversity on current projections on the planet will cause the global economy to be hit to the value of \$3 trillion to \$4 trillion by the end of the century. Has Treasury got any assessment of that cost of loss of biodiversity on the planet at current rates?

Mr Murray—Not that I am aware of.

Senator BOB BROWN—Would Treasury look at the *Guardian Weekly* report of that UN report which is coming out in October and give the committee its assessment of the biodiversity factor in assessing future economic wellbeing in a country that is losing biodiversity at one of the highest rates in the world.

Mr Murray—I will certainly take that on notice. Whether we have the wherewithal—the expertise—to do that is another matter. Certainly if we do then we will be able to supply an answer.

Senator BOB BROWN—As part of this population assessment—and we have talked about immigration—has Treasury done any assessment of the UN projection that there will be

150 million people moving on the planet and seeking other domicile by the year 2050 due to climate change alone.

Mr Murray—No.

Senator BOB BROWN—Would Treasury look at that figure and see if it can assess what impact that may have on Australia?

Mr Murray—We will take that on notice.

Senator BOB BROWN—Thank you very much.

[2.39 am]

Senator PRATT—I want to ask a question with respect to the discussion that we had before about child-care.

Senator BERNARDI—Are we on population now?

CHAIR—Yes.

Senator PRATT—Thank you. I understand that there was a Treasury working paper published in April on the responsiveness of female labour supply to child-care costs. This showed that the effects of child-care costs on labour supply were indeed statistically significant—I appreciate that this might not actually be your report—and on that basis is it true to say that changes—

Senator Sherry—Senator, sorry to cut you off, but that is actually for revenue group. It would have to go to revenue group.

Senator PRATT—If you would let me conclude the question you would find that it is not about the report necessarily.

Senator Sherry—I have just been advised that it needed to go to revenue group.

Senator PRATT—On the basis of what that report found, my question is: is it true to say that child-care costs could have a significant impact not only on birth rates but also on workforce participation rates in the future and thus mitigate the effects of an ageing population, particularly when we are looking at trying to keep in balance the ratio of workers versus those that the community supports?

Mr R Murray—Senator, I am not across that particular analysis. We could certainly take on notice where it relates to that analysis. Just from a general proposition, as I have pointed out previously and as Mr Gallagher has pointed out, at least the OECD studies and some country studies indicate that there is a positive relationship between participation and family-friendly policies, including child care. They also have a positive effect on fertility.

Senator PRATT—Great. Thank you.

Senator BERNARDI—I want to go back to the task force, and so I will go back to you, Mr Murray. You have 12 months worth of additional funding for the task force—\$1.3 million.

Mr R Murray—Yes.

Senator BERNARDI—Your reporting date is when?

Mr R Murray—We are anticipating probably about the middle of 2011—certainly in that first half of 2011. We are keeping it a bit flexible.

Senator BERNARDI—The minister has said that it is 12 months, which would take it to April.

Mr R Murray—Yes. I will put it this way: around about April.

Senator BERNARDI—You have funding for 12 months from June.

Mr R Murray—We have 12 months funding.

Senator BERNARDI—That is fine. What is the process of the consultation that you intend to undertake?

Mr R Murray—The minister and we are having discussions around all of that, so that has not been settled as yet. Certainly between the minister and us, we are making significant planning at least for the first stage of consultation. Prime Minister has in his press release made a commitment to an open consultation process, and that is our terms of reference on that.

Senator BERNARDI—Can you detail what the first round of consultations will be?

Mr R Murray—I cannot because that would be pre-empting decisions that the minister needs to make around that.

Senator BERNARDI—The minister has repeatedly said that 12 months is a very tight time frame to do this major task and that there was going to be a broad range of consultation two months into it. There has still been nothing decided. Is that what you are telling me?

Mr R Murray—No. I am not saying that the minister has not made decisions. He clearly has in his own mind and we have assisted him in coming to some of those decisions about what the first phase of consultation would be between now and, say, over the next six months, because we do need a significant amount of time in the first phase of actually getting across all the issues. You can hear from Senator Brown one side of all of these issues, and they are pretty complicated. There are a lot of trade-offs between a lot of the issues. So we want to have a reasonable amount of time over this first consultation period so that we can get all the issues on the table and all the issues discussed.

Senator BERNARDI—My concern is that there are a huge number of issues to be considered; it crosses over an enormous number of portfolio areas. There was clearly very little consultation before the announcement. There has been nothing concrete announced since the announcement by the minister. I am looking at his website. He has not put out one press release about it or anything else.

Senator Sherry—Your questions are going to the role of the minister. In terms of the minister, I know firsthand that, in gathering briefs, material and information in his own responsibilities, he sought—by way of example—a very significant set of data from the Australian Bureau of Statistics on population issues as well as face-to-face briefings. I know this because I have responsibility for the Australian Bureau of Statistics, so I signed off on the briefs and the documents. So that is an example of preparatory work. Just because a minister does not issue a press release does not mean that he is not focused on the job at hand.

Mr R Murray—I add to that that it is not as if we or the minister have been sitting around twiddling our thumbs. The minister has been trying to absorb as much information he can around this whole topic and having discussions and multiple meetings with a whole range of people. I am not quite sure how many, but it certainly must—

Senator BERNARDI—You would be able to take it on notice, wouldn't you—

Senator Sherry—I will take that on notice.

Senator BERNARDI—Who he has met with and the times he has met with them?

Senator Sherry—I do not necessarily believe we will be disclosing who he has met with. That is up to the minister. As you very well know, no ministers current or past in this place have disclosed their diaries. That has not been the practice. But I will take it on notice, and I am sure we can give you an indication of the—

Senator EGGLESTON—Posthumously!

Senator Sherry—Pardon?

Senator BERNARDI—The *Latham Diaries*. He helped us out!

Mr R Murray—We want to get to a position where we have a more structured program of consultations, and that is where the minister is moving. You are asking me to answer questions on the minister's behalf, and I just cannot pre-empt what he is going to say.

Senator BERNARDI—Time is short. Would you be to take on notice to undertake to provide me with the times and dates of briefings that your department has provided to the minister in regard to population policies?

Senator Sherry—Will take it on notice.

Mr R Murray—We will certainly do that.

Senator BERNARDI—Would you be to also take on notice and provide a list of key stakeholders that you consider in this debate?

Mr R Murray—What do you mean by 'that we consider in this debate'?

Senator BERNARDI—I mean those that you are going to include as part of the consultation process.

Mr R Murray—We can certainly take that on notice. Like every other part of advising, we are not the decision-makers in any of this. The fact that we consider somebody to be a key stakeholder is neither here nor there, quite frankly.

Senator BERNARDI—It certainly is important.

Mr R Murray—But we will certainly take this on notice and we will see what we can—

Senator BERNARDI—It is important because if you say that these are key stakeholders that you consider and the minister chooses to ignore those, that is the minister's decision. So it is important.

Mr R Murray—If you were to ask me what I thought were the groups of interests around this particular topic, I would say to you that you can just hear from the questioning today that there are significant environmental issues. Some people would consider that they should be

looked at in a more global sense, and that is pretty difficult. There are obviously issues around economic growth and industrial development around that. There are issues around food. There are certainly significant issues around the building, delivery, pricing et cetera of infrastructure.

There are obvious interest groups out there covering all of these areas, and they are the sorts of areas that we will need to cover off in any consultation. The consultation might cover the not-for-profit interest groups, various sectors of industry—some of them have differing interests in this issue—and certainly those, both public and private, who supply infrastructure and demand infrastructure. So there is a whole range of people from the private sector, the public sector and academia. We would want to try to cover off as much of that as we possibly can.

Senator BERNARDI—Okay. Has your task force been asked to undertake any modelling with regard to the population capacity of Australia?

Mr Murray—No, and I do not know that that is within the terms of reference. If you read the Prime Minister's press release carefully, he is talking about likely trajectories for population. He then asked us to look at the various constraints around that. I really doubt whether that gets you to some sophisticated modelling about what Australia's carrying capacity is. I think that is probably an impossible task because it is dependent on so many outcomes around things like climate change and productivity growth in various sectors, including the food sector. It is around a whole lot of things where you have to make assumptions that we are a small economy in a whole trading world.

Whether you can actually model those sorts of things, I do not know. There were those who thought that this planet could handle 6 billion, and now the UN numbers, as I understand them, have the population stabilising at 9 billion. Even 20 or 30 years ago, people did not think that was possible. Certainly, if you had said 50 years ago that there were going to be nine or 10 billion people on the planet people would not have believed that.

Senator BERNARDI—I guess that any kind of modelling out to 2050 cannot foresee all the ups and downs of the economic cycle or growth cycle, can it?

Mr Murray—It does not necessarily need to see the ups and downs of the economic cycle. This is the whole point of the discussion you had with Mr Gallagher about what level of migration we should be assuming. To do some averaging around that, rather than taking the top of the cycle, is actually very sensible. You do not necessarily have to do anything necessarily about cycles; you have to look at what the long-term trends are and what the sensible and likely long-term trends are. However, no matter what you come up with, I can assure you that it is not going to be right; but it may be in the ballpark.

Senator BERNARDI—We have seen that in the climate change modelling, and the furphies that have been in there. That is off topic, though, isn't it Minister?

Senator Sherry—That is off the topic, and it is also a political debate, so if you have got a question of relevance to the officer, please pose it.

Senator BERNARDI—No, it is not a political debate.

Senator Sterle interjecting—

Senator BERNARDI—Gee whiz, that would be the first intelligent contribution from you, Senator Sterle.

Senator STERLE—It's a replay of Q & A. You looked like a goose.

Senator BRANDIS—It will be a long time before you are invited onto Q & A, Senator Sterle.

Senator STERLE—That will not upset me.

CHAIR—Senator Bernardi is trying to ask his questions, Senator Brandis and Senator Sterle; can we have a little quiet.

Senator BERNARDI—I am surprised that Senator Sterle could start that one

Senator BERNARDI—Mr Murray, have you been asked to do any modelling to test the limits of the growth capacity of cities?

Mr Murray—No.

Senator BERNARDI—Is that going to be part of your terms of reference?

Mr Murray—I do not know. We will certainly be looking at what the tensions and constraints are going to be around, for instance, development of the cities. It is not pretty hard to guess that they have already got tensions, and a lot of the planning processes and the delivery of infrastructure have been pretty poor. There are a lot of issues, and a lot of policy issues to look at in relation to a lot of that.

Senator BERNARDI—I am trying to reconcile some of the statements that the minister has made with what you are telling me. He has said that your job is—he did not use the term 'carrying capacity of Australia'—'to test the limits of the growth capacity of cities.' Your responsibility is to come up with modelling and to say that this is where we would be under current things, and if you reduce that then this is where we would be et cetera. His job is to say where we should land. Ultimately, there is going to have to be a population target for Australia, isn't there?

Mr Murray—I do not know why you would come to the conclusion that we are going to have a population target. You may, at the end of the day, end up with scenarios that give you a sensible range about where we might land under sensible scenarios. We have already, out of our central scenario, given numbers about what might be the populations of some of our major cities. That certainly will then open up a whole lot of questions about what those cities look like and what the constraints are, but also about what the opportunities here are for making some sensible reforms and some sensible changes about the way we approach, for instance, urban development. But there are a lot of other issues as well. This whole debate is not just about the cities. There are a whole lot of different regions out there. Whether it is the major tourist towns and cities whether it is how we are going to cope with some of the resource towns and cities as well. There is a whole range of issues and a lot of it is different from region to region. We will try as best we can to at least measure some of that, but there may be limitations just within the data itself on a region by region basis. But we are certainly going to attempt, as far as we possibly can, to look at regional issues and to try and measure the population issues and the constraints there.

Senator BERNARDI—Mr Murray, we do not have any more time. I will put the rest of my questions on notice. If you could respond to them in as timely a manner as possible, that would be appreciated.

Mr Murray—I will.

CHAIR—Thank you. As there are no more questions on population, we will go to the afternoon tea break.

Proceedings suspended from 2.56 pm to 3.13 pm

CHAIR—Welcome back. The committee will resume. We are with fiscal group and Senator Cameron has a couple of questions.

Senator CAMERON—I wanted to ask about the total number of employees in the department.

Mr Murray—Our staffing numbers are around 1,000. At the moment, for instance, we have about 1,030 staff. On average for 2009-10 we are looking at about 1,000. At the moment we are a little higher because in February we had a very large graduate intake of 75. That is the largest intake we have had. But then with attrition over the year the average for 2009-10 is about 1,000. In the portfolio budget statement we have said 1,005.

Senator CAMERON—And what is your turnover of staff?

Mr R Murray—Up until 2009—and so impacting a lot on 2009-10—the attrition rate was somewhere around 12 per cent.

Senator CAMERON—Twelve per cent.

Mr R Murray—At times it has been lower than that, going back earlier in this decade, but for about three or four years, up to 2008-09, it was about 12 per cent. In 2009-10 it has actually fallen to about eight to 10 per cent. A lot of that, we suspect, is around the financial crisis and the state of the financial sector. Even though it has weathered the storm quite well, for a while the outlook in that sector was not good. That was reflected, again, in our graduate program. We took 75 graduates and all of them were of very high quality. We had, I think, over a thousand applicants—and a lot of them were of very high quality—again reflecting the downturn. However, the early indications for 2010-11 are that we think the attrition rate will return to about 12 per cent, something like that. That is what we are budgeting for.

Senator CAMERON—Generally, you cannot really make an estimate of who might resign or whatever. You might have an idea about your retirements, but your resignations are completely uncontrollable, aren't they?

Mr R Murray—They are. So what do we do? For 2010-11, we are trying to sort it all out in detail at the moment. We are budgeting, as set out here in the portfolio budget statement, for 1,010 staff. We will start the year with about 1,030 and we think that, with an attrition rate of about 12 per cent, we might lose 75 or 80 people during the year. So we look at it at a very high macro level. We are assuming at this stage that in February we will have another graduate intake of about 75, and through the year we have two fairly big what we call bulk recruitment rounds, where we might bring in five to 10 people in both those rounds from

outside the Treasury. That is the sort of planning we have got at the moment, and that is what our budget is built on.

Senator CAMERON—Are you a major employer of graduates amongst the Public Service in Canberra?

Mr R Murray—We are a major employer of top economists. An agency of 1,000 is probably reasonably big for a central policy department, but there are other departments that are much bigger than us. How big their graduate programs are, I am not sure. Certainly, we target the best economists that we can get but we also target lawyers because we have significant responsibilities in terms of tax and company law, competition policy and prudential and financial regulation. We do target commerce-accounting graduates as well.

Senator CAMERON—So you are looking at about a five per cent increase from where you are. If you could not do that increase and you were faced with a two-year freeze, you would be looking at 240 fewer employees in the department. How would that affect the operation of your department?

Mr R Murray—Just going to the start of your question, we are not budgeting for any increase. We are at around 1,000 staff, so 1,010 staff is around that.

Senator CAMERON—I thought you said you were going up, that was all.

Mr R Murray—No. We have grown a lot over the last decade, but we are now stabilised at around 1,000 and we are moving priorities. So we are around that level. With an attrition rate of about 12 per cent, on average we would probably lose about 75 to 80 staff a year. I have not thought about what it means over two years, I have to admit, and there may be some cumulative effect.

Senator CAMERON—There are proposals that there should be a staff freeze in the Public Service, so if you lose 150 staff and they are not replaced doesn't that have significant issues for you?

Mr R Murray—I will answer it this way: the graduate intake has traditionally been our lifeblood and, if we have difficulties around that graduate intake, that is always a problem for us. So in a year when the financial sector is going gangbusters, for instance, that might be a bleak year for us and that can be a bleak outlook then for our overall capacity.

We also have put more emphasis on our bulk rounds during the year bringing lateral recruitment in and we have also done a lot more recruiting at very high levels as well, getting in very specialised people—financial people, for instance, people that understand financial markets. We have some of those that have a detailed knowledge of the financial markets. So anything that interfered with any of those three would raise some issues.

Senator CAMERON—What issues would they be?

Mr R Murray—They are all issues around capability.

Senator CAMERON—What are those capability issues?

Mr R Murray—We need expertise in various areas about economics, about modelling, about the financial sector, about law and commerce, and if we do not have that expertise then our ability to produce outputs is a bit restricted. We always get by. We have in the past and

freezes come and go. I have been around a long time, Senator. Freezes do come and go and you do tend to have to adapt, but a two-year freeze would be pretty long.

Senator CAMERON—I am told that a two-year freeze has got implications longer than the two years because you have lost that recruitment of young graduates and then you have to try to play catch-up or you have to use contract input. Is that an option?

Mr R Murray—That has been so. When we have had lean years, that has been our experience.

Senator CAMERON—So when you have faced freezes before have you used contract to deal with it?

Mr R Murray—I am not sure that we have done that. Some other departments have.

Senator CAMERON—So savings that can be budgeted from reducing the head count might be diminished by bringing contract labour in to try to fill the gap created in key areas.

Mr R Murray—Yes, but I am not sure then what the objective of the freeze is.

Senator CAMERON—I am wondering the same thing, if in your experience in the past, contract labour has been brought in. But that is fine, thank you very much.

Senator JOYCE—Just before I start—and I know we have moved on from population—in the population assessment, Mr Murray, did you also look at what the development of regional areas would be?

Mr R Murray—Yes. We intend to do that and there are a lot of important issues. While you were out I did explain that. We do intend to look as closely as we can and it does not matter whether you define a region as out of Sydney or North Queensland or the Kimberley, for instance—

Senator Sherry—You should add Tasmania to that—

Senator JOYCE—West Coast.

Senator Sherry—I am in great agreement with you. Tassie has a population of half a million, significant surplus water, agricultural production, perfect climate, great people, including Senator Bushby—a fantastic place to live. I could just go on and on.

Senator JOYCE—Minister, this does not happen very often, but I agree with you entirely

Senator Sherry—Fantastic. I will make sure that Tassie is on that list—

Senator JOYCE—There is no reason to have a parliament at all; we are all in agreement. But what about all the infrastructure you are going to have to put in? I think it is a great idea. If you are going to have a population growth then have it in the regions, because there are exponential costs to growing cities, aren't there?

Mr R Murray—Not necessarily. Quite often public policy makers like to think that they can engineer a lot of this. But quite often a lot of this is driven by people's own choices and by economic forces. Whether you can engineer movements of population beyond that is always a difficult issue. There is always a difficult issue around regional development. However, having said that, sometimes there are efficiencies in doing regional development and sometimes there are efficiencies in having cities. Cities are highly efficient. It does not

mean Australian cities are highly efficient. Australian cities could be far more efficient. It is just from an economic point of view.

Senator JOYCE—If we look at the cost growth at the moment, we have just spent \$1.8 billion on a bridge in Brisbane and another \$2.2 billion on a tunnel. If that sort of investment or even a portion of that investment occurred in a regional area, surely you would have a vastly greater bang for your buck because you are on a greenfield area and you are not actually stopping the traffic and doing all these things to expand the infrastructure that is required.

Mr R Murray—That may be the case, but countering that there are a lot of opportunities within cities, some of them big, some of them limited, to use better the infrastructure that is already there.

Senator JOYCE—If we were prepared to stack one Perth person on top of another in flats, we could get efficiencies.

Mr R Murray—I do not look upon that as efficiency. The fact that we have cities that are very spread out makes us certainly, in the developed world, apart from the United States, fairly unique. There are a lot of different ways you can design a city. A part of what we want to do with this population strategy is try and look at some of the issues. If you are going to look at more efficient cities, for instance, you better look at how well planned they are and how good an environment you are creating for people. It is not about dumping people on top of one another.

Senator JOYCE—If you have going to have another five million people living in Sydney, I am sure the people of Sydney are going to be thrilled to hear that they are coming. In your analysis, are you going to do a comparative analysis between the cost of development of Sydney to deal with five million people as opposed to developing other inland regional areas to cope with the same population?

Mr R Murray—I do not know. I could not say at this stage.

Senator JOYCE—Can you explain to me what a growth dividend is, Mr Ray?

Mr Ray—A growth dividend is a colloquial term for a summary second-round impact of a major policy change.

Senator JOYCE—Of an imagined policy change?

Mr Ray—No, a major policy change.

Senator JOYCE—What is the growth dividend that is currently in the budget for the final two years of the forward estimates?

Mr Ray—You are asking the wrong group. That is why we are having trouble finding it.

Senator JOYCE—It is about \$600 million.

Mr Ray—It is about \$600 million.

Senator JOYCE—How do we get that money? Where does that money come from?

Mr Ray—That money comes from having a larger economy as a result of the measures in the package.

Senator JOYCE—A larger economy?

Mr Ray—Yes.

Senator JOYCE—From what?

Mr Ray—The government's tax plan. It is explained in the budget papers, in the first sentence of the measure description: 'The government's tax plan will promote growth across the entire economy.' That economy will provide a growth dividend in terms of higher tax receipts and lower—

Senator JOYCE—So the resource super profits tax makes the economy bigger?

Mr Ray—The modelling is that the tax package as a whole makes the economy larger.

Senator JOYCE—So this new tax is going to make everything bigger?

Senator Sherry—He did not say that. He just gave you the answer—the package as a whole, Senator.

Senator JOYCE—What part of the package makes the economy grow?

Mr Ray—You are talking to the wrong group, because we are not responsible for this package. I will try to help you a little bit, but you really need to talk to the experts. The lower company tax rate and the effective removal of royalties are the two biggest components.

Senator JOYCE—But the royalties are really just replaced by a federal government rent, aren't they?

Mr Ray—I think you have had long discussions with both Dr Henry and with the Revenue Group about this. Just to give you an example, when the royalty regime in Bass Strait was replaced by PRRT, the life and the production out of those wells was larger than had been expected under a royalty regime.

Senator JOYCE—What was the growth dividend we got from that?

Mr Ray—That measure was not large enough—

Senator JOYCE—To measure.

Mr Ray—to measure.

Senator Sherry—We can certainly take it on notice. In fact, I think it is a very good idea, Senator Joyce—

Senator JOYCE—Doesn't it seem a little bit fortuitous—

Senator Sherry—Just let me finish my answer.

Senator JOYCE—I have not asked you a question, so what is the answer?

Senator Sherry—You did.

Senator JOYCE—I have not asked you any questions, but I am glad I am about to get an answer to a question I never asked. I am fascinated as to what it will be.

Senator Sherry—Senator, Mr Ray has indicated that there was no modelling, no analysis done of that. I am sure there are other areas, such as when the PRRT was introduced more broadly across the economy and when the tax on the gold sector was introduced that Treasury

would have done some analysis. I am sure they were right. When we look back historically at the ridiculous and extraordinary claims made against those tax changes, if we do have any modelling analysis of those two measures, for example—I will take it on notice; we will get Treasury to scour their records—I am sure that their analysis turned out to be correct.

Senator JOYCE—You are very sure, aren't you.

Senator Sherry—History tells us Treasury was correct.

Mr Ray—I might just add that we have published material on how we have thought about second-round effects in the past—I think in the Treasury round-up a couple of years ago. While we accept that many measures have second-round effects, both the timing and the quantification of those is generally quite difficult. In the case of large packages it has been the practice for some time to come up with some estimate. It was done when the ANTs package, the GST package, was introduced and it was done in the Ralph business tax reforms.

Senator JOYCE—Seeing the minister is so sure, can the minister tell me what the growth dividend was from the petroleum resource rent tax? You are sure—you must know what it is.

Senator Sherry—What I am very confident of, as I have already said, is that the claims made by Treasury at the time would be accurate and—

Senator JOYCE—So you believe there was a growth dividend?

Senator Sherry—Can I finish my answer. I talked about the analysis, the projections. I did not specifically refer to the growth dividend.

Senator JOYCE—You did not refer to the growth dividend. You were not sure about the growth dividend, were you?

Senator Sherry—Can I finish my answer. If there is a growth dividend analysis of—

Senator JOYCE—If there is a growth dividend analysis—you are getting less sure by the moment.

Senator Sherry—If there is a growth dividend analysis as part of the overall analysis of the impact of those two particular measures I have just referred to, I am more than happy for Treasury to go through those records and come up with that analysis. As I have said, if you look at the analysis of those two particular measures which were introduced, particularly against some of the extraordinary, exaggerated claims that were made at the time by those who claimed they were going to be hurt by those two measures, I am very confident that the Treasury analysis would have been accurate.

Senator JOYCE—I am glad, Minister, that in the space of 90 seconds you have gone from 'sure' to 'if'.

Senator Sherry—No, I am sure of the—

Senator JOYCE—The question is 'if'. So let us go to the question 'if'—

Senator Sherry—Do not verbal me. I have been around long enough to know and I have been around long enough to know that I can be allowed to complete my answer.

Senator JOYCE—It seems fortuitous that we would have this notional revenue in the time that we need a surplus.

Senator Sherry—Can I complete my answer?

CHAIR—Certainly, Senator Sherry.

Senator Sherry—Thank you.

Senator JOYCE—To which question? To which question, Minister, are you repeating the answer to?

Senator Sherry—You just attempted to verbal me. You said ‘if’. What I am saying is that I am very confident that the Treasury analysis of the two measures that I have referred to, PRRT and the taxation of gold, is accurate. I am very confident of the analysis and the forecasts, if that included a second-round effect. I am very confident that the analysis, projections, commentary and forecasts—the whole package, if you like—was right. I am very, very confident, particularly in contrast to these extraordinary claims—

Senator JOYCE—I have not got a clue as to what question you are currently answering, but you are certainly occupying a lot of time doing it.

Senator Sherry—I am just finishing my answer. You pose these questions.

Senator JOYCE—If this is your tactic to not answer questions just come out and say so.

CHAIR—Senator Joyce, I think if you allow the minister to finish quickly, you can move on.

Senator Sherry—As I said, I have great confidence that the Treasury analysis at the time—compared to the extraordinary claims about the destruction of industry, the sky falling in and the industry disappearing et cetera—was correct.

Senator JOYCE—Can you tell me what the question was that you were just answering then? What was the question? Where did all that palaver come from?

CHAIR—Senator Joyce, would you like to go on to your next question now, please, rather than—

Senator JOYCE—I want to ask questions that get answered, not have answers given to questions that were never asked.

Senator CAMERON—Like: why was I sacked?

CHAIR—Senator Joyce, I would suggest that you cease the habit of rephrasing people’s answers in the way in which you prefer.

Senator JOYCE—This is the Labor Party tactic; here it comes.

Senator Sherry—We have all the witnesses here—expert witnesses. Senator Joyce should just stop wasting time and allow the witnesses to get on with giving their answers.

CHAIR—Senator Joyce, your next question, please.

Senator JOYCE—You are incredible! Is this growth dividend consistent with the underlying economic assumptions on which the projected budget outcomes are based?

Mr Ray—The growth dividend comes from the measure, and it is consistent with the modelling that was commissioned from KPMG Econtech.

Senator JOYCE—So the growth dividend is consistent with which KPMG report?

Mr Ray—The report that you discussed with my colleagues yesterday.

Senator JOYCE—Which is the?

Senator Sherry—This is the one that we discussed yesterday, Senator Joyce. I am just trying to be helpful.

Senator JOYCE—There are two KPMG reports. As you would know, Minister, there are two KPMG reports out at the moment, aren't there?

Senator Sherry—Yes. This is the report of 30 April 2010, extended 14 May. We believe that is the report.

Senator JOYCE—There is another one out at the moment. You are aware of that, aren't you?

Senator Sherry—No, I am not.

Senator JOYCE—Well, there is. It was put out by KPMG for the mining sector. It shows completely different outcomes.

Senator CAMERON—That is the Minerals Council. He who pays the piper, eh?

Senator JOYCE—I will take that interjection. Who paid for the first report? Senator Cameron has just said, 'He who pays the piper calls the tune.' So who paid for the KPMG Econtech report, Mr Ray? Who paid for it, Mr Ray? Who paid for that report? Who paid for that report—the first one, Mr Ray?

Mr Ray—You are asking the wrong person—

Senator JOYCE—Minister, who paid for that report? I am following up an interjection from your colleague, Senator Cameron. Who paid for that report?

Senator Sherry—It is revenue. I will have to take it on notice for revenue.

Senator JOYCE—You will have to take that on notice? Did the government pay for it, Minister.

Senator Sherry—Certainly I accept that the government paid for it.

Senator JOYCE—The government paid for it. You heard Senator Cameron say, 'He who pays the piper calls the tune.' Did you hear him say that?

Senator CAMERON—That is Mitch Hooke that does that, you know, those people who have got you in their pocket. The Minerals Council have got you in their pocket.

Senator JOYCE—Don't you agree that many, perhaps most, major policies of government have any effect on economic growth?

Mr Ray—I think I have already answered that question, Senator. We agree that many policy decisions have second-round impacts on the economy which feed back through to the budget. A lot of those effects can be negative. Were we able to quantify those and put reasonably reliable estimates on them, then we would do so when we cost revenue measures, and our colleagues in the department of finance would do so when they cost expense measures. For the reasons that we have put on the public record time and time again, that is an inherently difficult exercise for smaller measures. In the case of larger packages that they

have tended to be, we have put estimates on the so-called growth dividend, and I gave you the two examples of the Ralph tax package and the ANTS package.

Senator JOYCE—Let us come up with another substantial package. What about the \$16.2 billion you spent on halls and other eclectic tokenistic rubbish around the back of schools? What is the growth dividend from that?

Senator Sherry—Really, Senator!

Mr Ray—Again, Senator, I think you should be asking my colleagues from the Macroeconomic Group. Estimates have been published on the impact of the stimulus package on the economy and they are in the budget papers.

Senator Sherry—Senator Joyce, we had a discussion about this this morning in Macro, as I recall.

Senator CAMERON—You should get your act together.

Senator Sherry—You continue to waste time, Senator Joyce, with incessant repetition of questions.

Senator JOYCE—On a point of order, Madam Chair: this is merely a tactic by the Labor Party to answer a non-existent question. Minister Sherry is very good at it. He goes on with a dissertation to gobble up time.

CHAIR—I do not think you need to continue.

Senator Sherry—My contribution then was very brief. I was just pointing out he has already asked the question in Macro this morning and he is wasting time.

CHAIR—Mr Ray, do you have anything more to say.

Mr Ray—I will try to help. Again, you should be asking the relevant people, but when the economic forecasts were put together for the 2009-10 budget I am confident that they took into account the impact of that sort of direct public investment.

Senator JOYCE—Could you have an anti-dividend on a certain program? If you get a growth dividend can you get a growth shrinkage, or however you like to term it?

Mr Ray—Sure. You can have a policy which distorted resource allocation and you have lower growth.

Senator JOYCE—A distortion of resource allocation? Do you think that investing \$16.2 billion in overpriced school halls is a distortion of resource allocation?

Mr Ray—You have to think about the economic conditions at the time. There was a deficiency of aggregate demand. In a world in which you have a deficiency of aggregate demand, providing a stimulus to aggregate demand is not likely to be distorting.

Senator JOYCE—What period of time was that, when there was the deficiency in aggregate demand?

Mr Ray—At the beginning of 2009.

Senator JOYCE—So why are we still spending the money now?

Mr Ray—The program has time to run, Senator. As you discussed with Dr Gruen earlier today, the contribution to growth from the stimulus withdrawal is negative.

Senator JOYCE—So it would be fair to say that if this is a misallocation of resources we could be getting an anti-dividend or a shrinkage from the building the school hall revolution package?

Mr Ray—The contribution to growth of the stimulus package I think turns negative in 2010. Again, you discussed this at length with my colleagues.

Senator JOYCE—Is there anywhere else the growth dividend is on except your resource super profits tax—not yours, but the governments?

Mr Ray—The growth dividend is on the tax package, and the two major components that contribute to that are the reduction in the company income tax rate and the resource super profits tax.

Senator JOYCE—It is nowhere else to be found in the budget?

Mr Ray—As I have said to you, we do not deny the fact that all sorts of policy measures taken by governments over the years have effects on the economy, either negative or positive. Generally speaking, those second-round effects are difficult to quantify and to put timing on, as a result of which they tend to get taken up. Those effects get included in the budget through just the general process of forecasting economic activity and flowing it through to revenues and expenses. But, for some time now, where there are major changes that will affect resource allocation in the economy, successive governments have estimated a growth dividend.

Senator JOYCE—You would agree that the surpluses that are prescribed or projected in 2013-14 in the scope of things are extremely slim.

Mr Ray—I think the 2012-13 surplus projected is 0.1 per cent of GDP which, as Dr Gruen described it, is small; in 2013-14 it is 0.3 per cent. It is not the first time we have projected those sorts of surpluses, though.

Senator JOYCE—How did you go? Once you had projected them that far out, did you arrive at those surpluses or did you come up with a different number?

Mr Ray—Do you mean when we got to the year?

Senator JOYCE—Yes.

Mr Ray—If you have looked back over the past decade you would have seen that we tended to have outcomes that were larger.

Senator JOYCE—So you would be pretty confident that we are going to hit that billion-dollar surplus?

Mr Ray—No.

Senator JOYCE—You are not confident?

Mr Ray—We are confident that it is the best estimate that we have at the moment.

Senator JOYCE—So what is generally the discrepancy between what is projected three years out and what is actually achieved?

Mr Ray—In terms of what?

Senator JOYCE—We can look back for this government. I remember them talking about a \$17.7 billion surplus and we ended up with a \$57.1 billion deficit.

Senator CAMERON—Because of the global financial crisis—don't you remember?

Senator JOYCE—So how are we going in recent times, in the term of this government, in actually hitting the mark?

Senator CAMERON—It is no wonder they put Andrew Robb in.

Mr Ray—I think that is a matter for others to judge. I think Senator Cameron is saying that, where economic conditions change, you should expect that the fiscal outcome would change and, where there has been a policy change, the fiscal outlook will change.

Senator JOYCE—Do you see anything on the horizon on the moment that would change the outgoing numbers?

Mr Ray—As I said to you, these are best estimates at the time.

Senator JOYCE—So these take into account the current turmoil in Europe?

Mr Ray—Yes, they do.

Senator JOYCE—They do—good. So if things carry on the way they are going in Europe at the moment we can still expect to get a billion dollar surplus?

Mr Ray—If things turn out differently from what we are forecasting, then we will likely get a different outcome.

Senator JOYCE—What if things change in the negotiations that apparently the Prime Minister is engaging in with the mining sector? Will that change the surplus?

Senator Sherry—You posed that question. It is a repetition. I did indicate to you that, in terms of policy issues—

Senator JOYCE—Table 6 on page 313 of Budget Paper No.1 shows that policy decisions—

CHAIR—Senator Joyce, the minister has not finished his response.

Senator Sherry—Issues relating to the Prime Minister, or the Treasurer for that matter in the case of economics estimates, we will take on notice. It is not for Mr Ray to respond to a question like that and you know that.

Senator JOYCE—Table 6 on page 313 of Budget Paper No.1 shows that policy decisions since the 2009-10 budget have increased net spending by \$5.9 billion. That is the sum of policy decisions for the years 2009-10 through to 2012-13. That figure includes new spending measures, new taxes, saving initiatives. It shows that all the new taxes have been spent, all the saving initiatives have been spent and, on top of that, an additional \$5.9 billion has been spent for good measure. Policy decisions have not contributed in net terms to a single cent to reduce the deficit. Would you agree with that statement?

Mr Ray—I would prefer to answer it by saying that the reconciliation table on page 313, which is table 6 that you are looking at, gives an incomplete picture because, at the time of the

2009-10 budget, there was not the last forward year, which is 2013-14. That is one difference. Secondly, the numbers that are published in that reconciliation table include spending which would already have been allowed for in the contingency reserve.

Senator JOYCE—Spending which would already have been allowed for in the contingency reserve?

Mr Ray—Such as overseas aid and drought relief. If you look at page 3-7, table 3—I am not quite sure where the title came from—that shows the net budget impact in cash terms of policy decisions taken since MYEFO. Across the five years 2009-10 to 2013-14, the net impact is a save of \$544 million. I do not have MYEFO with me—someone else might—but there is a similar table that is published in the Mid-Year Economic and Fiscal Outlook which, I think, again showed that, once you adjust for the contingency reserve offsets to policy decisions, the policy decisions were a net save.

Senator Sherry—I am more than happy for Mr Ray and you, Senator Joyce, to continue, but I have to point out that the issues you are currently discussing—indeed these very tables—were discussed in finance in great depth.

Senator JOYCE—Mr Ray, do you see the position being more a result of good luck than of good management?

Mr Ray—I think that is question of judgment. But, if you are asking me: ‘Has the government delivered on the fiscal strategy that it set out in the Updated Economic and Fiscal Outlook in February 2009, repeated in the budget, the MYEFO and in this budget?’, I think I can say that there was quite a strong case made in the budget papers to show that it has.

Senator JOYCE—Has Australia ever had a bigger deficit than it had in 2009-10?

Mr Ray—As a proportion of GDP?

Senator JOYCE—As a raw number.

Senator CAMERON—Senator Joyce, no wonder you got the flick.

Senator JOYCE—We will go to both then. Mr Ray, tell me if we have ever had it bigger—in a raw number—and tell me the previous time that we had it that big as a proportion of GDP.

Mr Ray—I think the short answer to that question is: I suspect that in nominal dollar terms it is the largest deficit. In terms of a proportion of GDP, the problem we have is that we do not have underlying cash balance data that predate 1970-71. So I do not know what it was. During the Second World War, for example—

Senator JOYCE—Is there a bigger one back to 1971?

Mr Ray—I think not, but I would need to adjust it for Future Fund earnings and I have not done that calculation. But I think not. It would be a close-run thing to cite earlier ones.

Senator JOYCE—Do you want to inform Senator Cameron and me about when you thought you might have had a bigger deficit, in percentage terms, than what you had this year?

Mr Ray—As I said, I am not quite sure, but potentially it was during the Second World War.

Senator CAMERON—Another crisis.

Senator JOYCE—Almost as big a crisis as Kevin Rudd was the Second World War. I have to admit that.

Senator CAMERON—Or Barnaby Joyce as finance spokesman.

CHAIR—Senator Joyce, do you have another question?

Senator JOYCE—I do. I have a heap.

Senator CAMERON—Tell Andrew Robb that a lot of them have been asked—

Senator JOYCE—Chair, do you want to control your colleague?

CHAIR—Yes, well. He is silent now, so would you like to go on with your question?

Senator JOYCE—In 2010-11, the estimate is a \$41 billion deficit. Given that the Reserve Bank has recently been increasing rates to ward off inflation, is this prudent?

Mr Ray—I think the answer to that question is that in the first place the contribution of fiscal policy to growth in 2010-11 is negative; secondly, the fiscal consolidation from the peak deficit and this cycle, that is in the budget, is the largest fiscal consolidation on record. It then becomes a matter of judgement—should it be slightly larger or slightly smaller. That is really a policy question that you would need to ask others about. But it is the sharpest consolidation across a four-year period since 1970-71.

Senator JOYCE—Seeing as it is the largest deficit in both raw numbers and percentage terms since 1971, if not since the Second World War, what is our gross interest expense at the end of 2012-13?

Mr Ray—The answer to that question is in the budget papers.

Senator JOYCE—I know.

Mr Ray—Gross interest on all financing costs is \$13.8 billion.

Senator JOYCE—On a \$222 billion gross debt?

Mr Ray—I think it is better to look at it as a proportion of the economy, so I suppose it is about one per cent.

Senator JOYCE—I am trying to work out the cost of funds.

Mr Ray—Yes, \$232 billion

Senator JOYCE—And you have \$13 billion in interest, so you are getting your money at about 5½ per cent, is it? That is not meant to be a smart calculation—

Mr Ray—No; I can help you here. In terms of new issuance, the budget assumption is for a cost of funds of about 5½ per cent. That is the weighted average cost. I think Senator Bushby and I have discussed this several times.

Senator JOYCE—Do you believe that is what we are actually going to be paying for money at that point in time, considering what is going on around the world?

Mr Ray—Again, as we have discussed on many occasions, we use an assumption of our interest rates in the budget rather than market rates, because we do not think we can second-guess the market.

Senator JOYCE—So you take the interest rates from now to work out what you are going to pay as a cost for funds in two years time?

Mr Ray—For the new issuance—for existing stock we know what the cost of funds is as we have already issued it—we take the yield curve just before the budget, we look at what that implies given issuance strategy for the weighted average cost of funds at that time, and then we apply that across the forward estimates. That is not an unreasonable thing to do because at that time, particularly when you are talking about longer rates, the market will have taken into account in its assessments its perceptions of forecast expectations of future developments across that period, and they will be built into the yield curve.

Senator JOYCE—Do we extrapolate the yield curve out, or do we rule it off and take it at that spot.

Mr Ray—We take what the yield curve is at that time, and we use that as a technical assumption across the budget.

Senator JOYCE—But it is not being outrageous to say that the trend in the yield curve and the cost of funds is up.

Mr Ray—I do not think that is borne out by the evidence at the moment. The yield curve moves around, but the weighted average cost of funds taken out of the yield curve at MYEFO was about 5½ per cent. It turns out that by the time we got to budget and we did the same calculations it was about 5½ per cent. Since that assumption was struck, it turns out the yield curve has actually moved in.

Senator JOYCE—In the underlying cash balance, can you please explain the line ‘Add contingency reserve offsets to policy decisions.’

Mr Ray—Yes. Governments over many years have included in their contingency reserves allowances for various things. The two big ones in this context are the aid program and exceptional circumstances relief for drought. When the government takes decision to spend aid money, money is taken out of the contingency reserve, so the impact on the underlying cash balance of that decision is zero. That line is where the funds were provided for in the contingency reserve and the government has subsequently taken a decision to spend it. That is the offset. The net impact of those decisions on the underlying cash balance is zero.

Senator EGGLESTON—I would like to move on to a different subject, which is developing and monitoring programs. The fiscal group has responsibility within Treasury for policy development in education, and its mission statement is ‘to ensure government spending arrangements are effective’. First of all, I would be grateful if you could explain the department’s role in relation to the Building the Education Revolution, a program that had a \$1.7 billion blow-out, and its effectiveness has been questioned around the country. What was your role in developing that program?

Mr Ray—We provided advice to the Treasurer during the course of that policy’s development.

Senator EGGLESTON—How long was the Treasury given to analyse the policy and provide advice. How long did you have to do this?

Mr Ray—The policy was announced in the first week of February 2009. The policy development work around that package commenced in 2008, but whether that particular component of that package—I would need to take it on notice.

Senator EGGLESTON—What was the department's understanding of how the policy had been costed? How were costs worked out? Was there an average? Did you think there might be a mean figure that could be applied for most of these buildings and so on?

Mr Ray—Unless my colleagues have something to add, that was really a matter for Finance and the education department.

Senator EGGLESTON—Was the department aware of the need for the extra \$1.7 billion that was subsequently required.

Mr Ray—When, Senator?

Senator EGGLESTON—A question of timing? Were you monitoring the expenditure?

Mr Ray—We do not monitor expenditure. We became aware at some point that there would be a need. There were further processes involving cabinet around that, and a package was announced where changes were made to some elements of the UEFO package that offset the need to vary the estimates for Building the Education Revolution. In the process of the development of that package, you could expect that we provided advice.

Senator EGGLESTON—I would expect that. I am trying to tie it down to a point where you might have become aware that there would be a need for extra funding presumably prior to you working out some sort of submission to present to cabinet. Is it possible for you to give some sort of indication of when it was you first became aware that there was a problem that needed to be addressed.

Mr Ray—I do not want to mislead you. I do not know that we did make a submission to cabinet.

Senator EGGLESTON—You did not say that; I said that, I agree. I was trying to be helpful!

Mr Ray—I can take it on notice and see if we can provide any particular dates. I think the general answer is that quite clearly you would expect, given that we are likely to provide advice to the Treasurer ahead of cabinet discussions, that at some point we became aware.

Senator EGGLESTON—We are interested in what some point is. If you could assist the committee with an answer on notice, that would be very helpful.

Mr Ray—I know you are interested in what that some point is and I will take it on notice.

Senator EGGLESTON—Obviously the department's advice was sought about the need for additional funding and I presume the department's advice was that additional funding should be provided for this program. Or was that not it?

Mr Ray—That is going to what our advice was. I am happy to take it on notice but, as you know, it would be very unusual for it to be provided.

Senator EGGLESTON—We would be interested to know how you felt the program was going.

Senator Sherry—I love the way you say you would just be interested to know. Mr Ray has made the position clear. It is advice to the minister.

Senator BUSHBY—You could provide the answer in accordance with the orders of the Senate.

Mr Ray—I said I am happy to take the question on notice.

Senator Sherry—I am more than happy for the question to be taken on notice.

Senator EGGLESTON—All right, we will have that question on notice. We move on to stage 2 of the program where additional funding has been provided. What was the department's ongoing role in that phase 2 stage? How did the department monitor the program if at all?

Mr Ray—As I said earlier, we do not monitor programs.

Senator EGGLESTON—But surely if there had been a failure in stage 1 of the program and additional money was required, you might have been interested to know how stage 2 was progressing, if we can call it that, and whether or not you might have had to provide further additional funding for example.

Mr Ray—I do not want to provide comments but I do not want to accept that there was a failure in what you call stage 1 of the program just because additional funding was needed. It is not unusual for estimates to be varied for programs.

Senator EGGLESTON—I suppose that is the case but \$1.7 billion is quite a lot of money to suddenly find you need to keep the program growing. I would have thought you would notice if you were short of \$1.7 billion?

Senator Sherry—Mr Ray has clearly indicated the responsible department is DEEWR and the Department of Finance and Deregulation certainly would have had some oversight view but not Treasury. Treasury would have been asked their view, as Mr Ray has indicated, by the minister and that would have been advice to the minister. Beyond that, Treasury do not oversight program by program expenditure.

Senator EGGLESTON—I understand that. I suppose where there is a need for an extra \$1.7 billion dollars, as I have said three times before, that would have attracted a certain amount of interest in Treasury.

Senator Sherry—It was indicated there was clearly interest. When Treasury asks for a brief from any department about anything I am sure they get a very quick response. But it is not the role of Treasury to oversight specific expenditures in other departments. Finance does have a role.

Senator EGGLESTON—Finance does have a role, I agree—very much—but I would have thought that, around the coffee table at morning tea, someone might have said that \$1.7 billion—

Senator Sherry—Again, you are—very courteously, I have to say—attempting to find some other mechanism by which Treasury oversight expenditure. As sure and confident as I

am that they do discuss issues from time to time, over morning and afternoon tea, and over lunch and dinner and everything else, it is not part of the formal process responsibility oversight of Treasury.

Senator EGGLESTON—We will accept what you are saying then, Minister, even though they might have discussed this at morning tea—

Senator Sherry—I am sure they discussed the relevance of questions at estimates and who is doing what. I am sure that is discussed over morning and afternoon tea.

Senator EGGLESTON—they are not prepared to perhaps assist the committee in its assessment of this program and what went wrong. But I might just ask: does the department think that Building the Education Revolution was value for money, as it turned out, in the way it was administered and good policy? Just say ‘value for money’. I know that policy is a difficult area for you.

Mr Ray—Senator, it is not our role to make such judgments. It would be reasonable for you to ask us whether we thought that the fiscal stimulus package was effective in a macroeconomic sense, and I think you have already had a discussion of that with our macroeconomic group colleagues. It is not our role to assess whether an individual program is value for money. That is a matter for others, including the Auditor-General.

Senator Joyce interjecting—I am aware of press reports to that effect.

Senator EGGLESTON—Well, I do not know. It was a \$16.2 billion program, I believe, and \$1.7 billion is quite a bit extra to require, so we find it a little bit surprising that you do not have an opinion about the effectiveness of the way the program was administered.

Senator Sherry—Senator, this is your second or third go at this question. The matter has been answered by Mr Ray previously and in another part of Economics, in macro. I am impressed by your ongoing courtesy, but no.

Senator EGGLESTON—Thank you so much, Minister. Let’s move on to another program then: the Home Insulation Program. Again, would you be good enough to explain the department’s role in relation to the Home Insulation Program?

Mr Ray—Senator, you can expect that we provided policy advice on the program.

Senator EGGLESTON—You did provide policy advice. That is very good. We know then that you provided policy. I wonder how long was given to you to analyse the policy and provide advice.

Mr Ray—I think the answer is fairly similar to the last program, because my recollection is—I may be getting the program wrong but someone will help me—that that program was part of the 3 February 2009 package. The policy development around that package we were definitely providing advice during that process.

Senator EGGLESTON—I suppose the real interest in this particular program has been the way it went wrong, isn’t it? It turned out to be a bit of a disaster, in fact, with concerns about the destruction of property, injury and loss of life, plus doubts that it was an effective form of stimulus. Will the Treasury be undertaking an analysis of whether or not there should have been more awareness of the problems and safety precautions taken?

Mr Ray—Senator, again I think that is a question for others. It is something Treasury obviously was very involved in developing policy—

Senator Sherry—It is part of the macro stimulus package, and Mr Ray has gone to that. The responsible department and, to some extent, Finance, are the relevant areas—but not the fiscal group of Treasury, Senator.

Senator EGGLESTON—Surely, though, there must have been some element of due diligence in recommending any program?

Senator Sherry—It is not an issue for the fiscal group of Treasury.

Mr Ray—Senator, you are also going to the nature of our policy advice.

Senator EGGLESTON—And of course it does to some degree but, in any policy advice, surely you would have some sort of due diligence factor on which you would assess possible risks and would want certain standards to be maintained. It seems that in this program perhaps those things did not occur.

Mr Ray—When we are providing policy advice we bring our comparative advantage to the table and there are other agencies which bring their comparative advantage to the table.

Senator EGGLESTON—Finally, I want to ask you some questions about funds that were allocated to the Department of Climate Change and Energy Efficiency in the budget. In the portfolio budget statement for that department, \$132 million was allocated to a program that no longer exists—the Low Emissions Assistance for Renters program. How did that occur? You managed to allocate \$132 million—quite a large sum of money in most people’s terms—to a program that no longer existed. I think, in some ways, it is a bit of an achievement to do that, but other people may regard it as gross negligence.

Mr Ray—My understanding is that a corrigendum has been issued correcting that. It would be a question more for the department of climate change; it is their portfolio budget statement, not ours.

Senator EGGLESTON—I agree that a correction was issued on the website, stating that the \$132 million was actually for a program called Green Start, a program to succeed or follow the bungled Green Loans scheme that was to help households reduce their energy and water use. Could you perhaps tell us what the \$132 million actually went towards. What is that \$132 million funding?

Mr Ray—Again, this is really a question for the department of climate change. It is not our program; it is their program.

Senator EGGLESTON—I agree it is not your program; but you are the funders—

Senator Sherry—Senator, if we were to accept questions on details of programs, the fiscal group of Treasury would be here all week and all night. We would have no other estimates hearings if we accepted—

Senator BUSHBY—These questions are to ensure that spending arrangements are effective. That is what these questions are about: the effectiveness of the spending arrangements.

Senator Sherry—That was not the question that was posed. The discussion and the questions remind me of, at least, some elements of the Finance estimates where Finance is expected to provide—and, to some extent, they can provide detailed knowledge of some programs in other departments because scrutiny is part of their overall responsibilities—but fiscal group in Treasury—

Senator BUSHBY—Has a specific responsibility—

Senator Sherry—I am sure if—

Senator BUSHBY—Do they ring you or read the portfolio budget statements?

Senator Sherry—I am sure if there is an area where they indicate they have done particular work, and that may be the case from time to time, but generally it is not going to be possible to provide that because it is not its responsibility.

Senator BUSHBY—Are you saying they do not even read the portfolio budget statements—

Senator Sherry—I did not say that.

Senator BUSHBY—relating to what is in the portfolio budget statement. They are responsible for ensuring that the expenditure is appropriately and efficiently outlaid.

Senator Sherry—I did not say—

Senator EGGLESTON—What Senator Bushby is saying is really at core and quite correct. What seems to be implied by this error is that, if a department puts in an application for funding for so-called program X and it happens to be for \$132 million, it is just ticked off without any assessment of what the program is, what it is designed to achieve and whether the expenditure is justified. Surely this is a matter of grave concern. It ought to be a matter that every citizen of this country should be worried about. Here we have Treasury just flicking money off to programs they do not know anything about.

Senator Sherry—That is not right.

Senator EGGLESTON—That seems to be the impression.

CHAIR—Can you allow Mr Ray to respond.

Senator EGGLESTON—I may be stating it in fairly gross terms.

Senator Sherry—Your courtesy is lapsing, and you are being somewhat argumentative and making an incorrect claim about the role of the fiscal group.

Senator EGGLESTON—Nevertheless, the fact remains that that is essentially true.

Senator BUSHBY—It is their mission statement.

CHAIR—Senator Bushby, you have made your point. Mr Ray.

Mr Ray—Your questions are proceeding on the basis of a misperception. The question of the entry of an estimate by a portfolio is a matter between that portfolio and the Department of Finance, not the Department of the Treasury. Our role in our mission statement is around providing policy advice, particularly when new policy proposals come before government. I

do not think you can leap to the fact that we should have been out there doing something about the fact that there has been an error in a portfolio's PBS.

Senator EGGLESTON—As I said, I would have thought there was some sort of due diligence requirement on behalf of the people of Australia that you would ensure that the programs you are providing money for actually do exist and that this is justified expenditure.

Mr Ray—We do not actually provide the money; that is the first point. The second thing is—

Senator EGGLESTON—You are the Treasury, as I understand it.

Mr Ray—The program estimates are matters for the relevant portfolio and agency and the Department of Finance, not for the Treasury.

Senator EGGLESTON—Finally, is the Treasury taking any steps to ensure that such errors do not appear in future budget papers? Are there any issues that you are going to look into regarding how your department prepares its statements?

Mr Ray—I will answer that in general terms. Yes, were it possible—presumably it is possible—to produce a complete set of budget papers without a single error in them that would be the ideal outcome. History suggests, though, that that is unfortunately not that likely. I have been around for only 20-odd years. If you look back at budgets over the past 20-odd years there may be one that does not have a single error in any of the documentation, but I would probably be surprised. After the budget every year we have what we call a 'postmortem', a detailed review of the whole budget process, which we do with our colleagues, the Department of Finance and the Department of the Prime Minister and Cabinet. We look at all these sorts of issues and see whether changes need to be made to our systems and processes to minimise the chance of a particular type of error recurring. We in the Treasury do not see the portfolio budget statements.

Senator Sherry—I have been here almost as long as Mr Ray. I can recall the first budget of the former government in 1996—that is a long time ago now—when the Department of Finance had to issue a corrigendum with, I think, about 70 or 80 errors. It went to pages of errors. It was somewhat embarrassing for them, but errors do occur from time to time. That is the worst I can ever recall, I have to say.

Senator BUSHBY—That was put together in a very short period of time after a new government was elected.

Senator EGGLESTON—That is right, too—three months, in fact.

Senator Sherry—Notwithstanding that, it was a very, very large set of errors. I am just pointing out that errors do occur from time to time. That is one that I can certainly recall, because it was an embarrassment to the Department of Finance at the time.

Senator EGGLESTON—I am sure it was, Senator Sherry, but the fact is that an error occurred, and the fact that postmortem meetings are held to look into the reasons for these kinds of failures occurring is encouraging.

Senator Sherry—Did you say 'postmortem'?

CHAIR—That is the term Mr Ray used.

Senator Sherry—I know you have a medical background!

Senator EGGLESTON—But to the average Australian \$132 million is an awful lot of money, and I think the Australian people would expect there to be a much more rigorous assessment of expenditure and of the allocation of expenditure than appears to have occurred in this case.

Senator Sherry—To the extent it is an important issue, and you are raising it, it should be raised with the appropriate department.

Senator EGGLESTON—I would have thought that Treasury was one of the appropriate departments, but I will leave the matter there.

Senator CAMERON—Senator Joyce raised the issue of growth dividend from the RSPT. Was there a growth dividend attached to forecasted tax collections related to the GST reform?

Mr Ray—When I was answering Senator Joyce's questions I referred to two previous occasions. One was A New Tax System package, which included the goods and services tax. The other package was the so-called Ralph package around business tax. On both occasions a growth dividend was included.

Senator BUSHBY—Looking at budget paper No. 1, page 9-23, note 15: can you explain what assets make up the 'Others' row in the presentation of the Commonwealth's holding of investments, loans and placements? I am interested in you providing a precise disaggregation of this 'other' row into all of its constituent elements such that there is no residual 'other' row. We are talking about \$60-plus million.

Mr Ray—I am happy to take it on notice to see what we can provide. It is mainly Future Fund holdings. We do not have a detailed disaggregation.

Senator BUSHBY—Anything else you are aware of, that you can give me today?

Mr Ray—The national building funds are in that line as well.

Senator BUSHBY—We are talking about \$60-plus million. It would be worth having another line that did not say 'Other' when you are looking at this—an awful lot of money that belongs to taxpayers of Australia. A little bit more transparency would be good.

Mr Ray—We can go back and have a look but I suspect it has been this way for some time.

Senator Sherry—We will take it on notice. I remember having a significant fight about the disaggregation from revenue for that surcharge measure. It took me four or five years to finally get it disaggregated, but we finally got it disaggregated.

Senator BUSHBY—Minister, I have enjoyed your reminiscing over the last two days of the year-and-a-half, I think you said, that you have spent in estimates. It is good to hear that it continues today; telling us all about your memories of past times.

Senator Sherry—It sounds like a reasonable suggestion; I will put it on notice. There has been disaggregation before, following the questioning of non-government senators.

Senator BUSHBY—On the previous page, 9-22, note 14 indicates that there is about \$13 billion in student loans on the asset side of the Commonwealth's balance sheet. How are these assets valued on the Commonwealth's balance sheet?

Mr Ray—This is the wrong portfolio. They are actually valued by the education department, not by us. They are valued at what is called 'fair value'. So they take into account things like—it is probably not that relevant this year but it will become more relevant in time—expected death rates of people who may have a HELP debt; they also use actuarial valuations. I do know it is called 'fair value' and it is done by the department of education.

Senator BUSHBY—'Fair value' is a technical term.

Mr Ray—Yes.

Senator BUSHBY—Is it a form of written down value to reflect the expected value of the repayments in the future?

Mr Ray—It does not include a provision for doubtful debts, that is in the other line. But it does include an estimate of mortality.

Senator BUSHBY—Do they consider the fact that generally student loans are only lifted at the inflation rate rather than at a commercial interest rate?

Mr Ray—Yes, they do.

Senator BUSHBY—On the assets side of the general government balance sheet, how much constitutes cash or the non-equity investments of the Future Fund, the Building Australia Fund, the Education Investment Fund or the Health Investment Fund?

Mr Ray—So the cash holdings of all those funds?

Senator BUSHBY—How much constitutes cash or the non-equity investments of any of those funds?

Mr Ray—I think it is best if we take that question on notice because the answer is quite detailed.

Senator Sherry—I think those details were provided at finance.

Senator BUSHBY—Okay, then it would probably be very easy for you to hunt them out and provide them to me. What is the justification for using these cash holdings of the Future Fund and other funds to offset gross debt?

Mr Ray—It is the accounting standard. I will go back a question. I can tell you the Future Fund's cash holdings at 31 March were \$10.5 billion. Its debt securities were \$14 billion.

Senator JOYCE—So how much is in other than that? How much of the \$62,925 million, or \$62 billion, is from the Future Fund?

Mr Ray—I think it is best if I take that question on notice, to make sure that we—

Senator JOYCE—It is definitely at 10.5 but there is also the other amount as well.

Mr Ray—Yes. Senator Bushby asked me what is the justification. It is consistent with the accounting standard.

Senator BUSHBY—I understand that the Building Australia Fund, for example, holds considerable cash due to imminent drawdowns for the government. But since these current liabilities are not recognised on the balance sheet why do we use them to offset our gross debt?

Mr Ray—Again, as I said, it is consistent with the accounting standard.

Senator JOYCE—Which accounting standard?

Mr Ray—I suspect it is ABS GFS.

Senator BUSHBY—And that treatment under that standard has been consistent for a number of years as to how you would show those relevant entries? Has anything changed in the last two or three years?

Mr Ray—It is safest if I take that question on notice.

Senator JOYCE—Can you just tell me though which accounting standard?

Senator BUSHBY—You have got the accountant very excited by mentioning accounting standards!

Mr Ray—Generally speaking, the budget is prepared using two accounting standards, AAS and ABS GFS, and there is a technical note towards the end of statement 9.

Senator JOYCE—What was the other ABS one? It would have a number, wouldn't it?

Mr Ray—ABS GFS and AAS.

Senator JOYCE—Number what?

Mr Ray—It is 1049.

Senator BUSHBY—How does the government define spending for the purposes of measuring the two per cent increased cap on real spending? That is, which expenditure line is used for this purpose?

Mr Ray—Payments for spending.

Senator BUSHBY—So that is it—payments for spending?

Mr Ray—It is cash payments.

Senator BUSHBY—What deflator does it use to calculate the real increase in spending?

Mr Ray—The CPI.

Senator BUSHBY—Looking at the budget, about \$976 million of funding under the nation building program has been brought forward to this financial year. What was the rationale for bringing forward these payments?

Mr Ray—That is really a question for the department of infrastructure.

Senator BUSHBY—That is fine. I will move on. Did you receive any requests from states to bring forward these payments? Are you aware of whether the government did that through you?

Mr Ray—Again, I think the question of the programming of those payments is a matter for the department of infrastructure.

Senator BUSHBY—Are you aware of the answer to that question?

Mr Ray—No. I am not aware of the answer to the question.

Senator BUSHBY—Are you aware of the answer to the previous question?

Mr Ray—No. I am not aware of the answer to the question.

Senator BUSHBY—You are not aware of what the rationale was for bringing forward the payments?

Mr Ray—I think it is best to ask infrastructure.

Senator BUSHBY—Are you aware of the reason?

Mr Ray—No.

Senator BUSHBY—Are you aware of the reason, Minister?

Senator Sherry—No.

Senator BUSHBY—Is it normal practice for funding to be delivered to the states so far in advance of their expenditure needs?

Mr Ray—Again, you are going beyond our expertise, but the practice of when payments go to the states varies from program to program, project to project. They tend to be set out in individual agreements with the states on a project by project basis. Some have milestones; some have different forms. It is also not unusual for the timing of those payments to be varied during the life of the program.

Senator BUSHBY—Would the timing of those payments in those not unusual circumstances be varied in circumstances where the states do not actually need the money at that point?

Mr Ray—I think it is best to say that payments to states have been brought forward from time to time over the years. It is not an unusual thing to happen. Whether the states can use the money is a different question.

Senator BUSHBY—In terms of due diligence and the approach that you have to making payments to states under agreements that you have with them, do they have to show they need that money to pay for the program they are delivering? Are there any criteria that need to be met?

Mr Ray—I will start and Ms Vroombout can help me if I get into trouble. The individual agreements have different forms of scheduling the payments. Sometimes they are subject to milestones; sometimes they are paid on particular predetermined dates. In terms of our role in making payment to the states, we would act on the advice of the relevant agency that the agreement had been satisfied. Obviously if the agreement is that the payment goes on the first payment day after 31 March, it is fairly easy to see that has been satisfied. If it is a payment that is subject to certain milestones then it is a matter for the relevant agency to instruct us to make the payment.

Senator BUSHBY—If the infrastructure department comes to you and says, ‘We would like the billion dollars we were supposed to get next year,’ you would say, ‘Not a problem, if

that's what you need, we'll give it to you.' You would not go through any due diligence check or ask any questions?

Mr Ray—No, it would not work like that. It would need to be consistent with the agreement with the state.

Ms Vroombout—In making payments we require certifications from portfolio agencies that the payment is consistent with the agreement. Each month when we make a payment we receive certifications from portfolio agencies that the payments are authorised by agreements with the states.

Senator BUSHBY—And that is all it says? They say to you, 'This is authorised by the state.' You do not need to see the agreement. There is no sort of monetary limits. We are talking here about \$1 billion. You do not have any thresholds at which you would take a closer look rather than just accept a single page certification that this is in accordance with what we agreed with the states.

Ms Vroombout—We do do some quality assurance of payments to the states and check against agreements that we hold.

Senator BUSHBY—In this case, where the budget shows almost one billion has been brought forward, you have not employed that quality assurance process to ensure that this request to bring forward a billion dollars is in accordance with the states?

Mr Ray—We need to be careful, but we are happy to see if we can add anything. We do not think the payments have been made yet.

Senator BUSHBY—I do not think they have either. There was a note in the budget that they would be. When the budget measures are put together, noting that this billion dollars has been brought forward, or a large amount of money has been brought forward from when it was anticipated being spent to an earlier year, is that something that the fiscal division would have an interest in?

Mr Ray—To the extent that we have an interest in putting the budget together, of course we have an interest.

Senator BUSHBY—Presumably somebody has come to you and the department of infrastructure saying they want to spend the \$976 million this year rather than next year?

Mr Ray—There are movements of funds backwards and forwards across the budget across a whole range of portfolios throughout the budget process.

Senator BUSHBY—I acknowledge that. Presumably you do not just act as a bookkeeper; you actually take a little bit more of an interest in it and if somebody is moving a billion dollars forward, you would actually take a bit of a look at it—

Senator Sherry—You used the word 'interest' in your question. I think you could take that a couple of ways. I think it is fair to say Treasury has an interest in everything—

Senator BUSHBY—Mr Ray has indicated he is not aware of the rationale for it being brought forward.

Senator Sherry—Let me just finish. Treasury has an interest in everything—a general interest in anything and a specific interest from time to time. But direct interest, I think, would be a different thing from a general interest—

Senator BUSHBY—But this is the Fiscal Group and their remit is to oversee the spending of the money that the government spends. Here we have a billion that was set to be spent in one year and now it is being brought forward to be spent one year earlier.

Senator Sherry—I think this goes back to our earlier conversation about the role of the Fiscal Group. Where there are officers that can help you in the general, if they are not aware of the specifics, they will certainly try to help you, but there is a limitation on the level of detail that Fiscal can go to in some of the circumstances you are raising.

Senator BUSHBY—Mr Ray has indicated that he is not aware of the rationale for bringing it forward. Is anybody in the room aware of the rationale for bringing it forward?

Mr Ray—If you look at page 272 of Budget Paper No. 2, \$44 million has been brought forward for the Douglas Arterial Road. It says:

The Government will bring forward \$44.0 million to 2009-10 ... to accelerate commencement of work on the project.

So, I assume that is the reason. For the Holbrook bypass, it says:

The Government will bring forward a payment of \$201.5 million to 2009-10 ...in order to facilitate early commencement of the project.

For the Ipswich Motorway, it says:

The Government will bring forward \$500.0 million to 2009-10 ... to reflect the progress made on the project to date.

For the Superway and Northern Expressway, it says the government will bring forward funds 'to facilitate the early commencement of construction as part of the South Road package of works'. There is also \$6 million being brought forward for the completion of a project. So, if you go through the budget papers, in each case the reason for the bring-forward is set out.

Senator BUSHBY—So we have worked out the rationale is to bring forward, in most cases, the early commencement of these projects.

Mr Ray—Or because of early completion, I think. Again, it is going beyond our expertise. The reasons are set out for each of them.

Senator BUSHBY—Are you aware of whether the states requested that these be brought forward so they could start the early commencement?

Mr Ray—You have asked that before, and I am not aware of whether the states requested it.

Senator BUSHBY—The budget also brings forward \$500 million in local government funding. Are you aware of what the rationale was for bringing forward over half a billion dollars in local government funding?

Mr Ray—Not off the top of my head.

Senator BUSHBY—These payments were brought forward last year as a stimulus measure. Now that we are moving towards trend growth, why are they being brought forward now.

Mr Ray—It is not our portfolio, but I can read to you from the budget papers. It says: ‘to ensure that councils have immediate use of these funds. This will ensure local government is able to take maximum advantage of the global recovery.’ And ‘improves their financial capacity and assists them in planning their works programs.’ Again, these are questions that you should ask the Department of Infrastructure, Transport, Regional Development and Local Government.

Senator BUSHBY—Okay, so it is giving them funds earlier. That is a desirable thing at any time. It is interesting that there is no sort of steel to that rationale. It is more just a group of words put together that really does not say very much at all. Giving them the money earlier; why not bring forward—

Senator Sherry—As to the detail, further explanation and exploration, it is the department, Senator.

Senator BUSHBY—Okay. You are not aware whether the local government has requested that money to be brought forward early?

Mr Ray—No, Senator, but local governments generally request money.

Senator BUSHBY—I am sure they request money. An Australian National Audit Office report on Roads to Recovery expressed concerns about the cost of the government making advance payments to local government. Did you look at that report before bringing forward this spending?

Mr Ray—A, we did not bring it forward. It was a decision of the government—

Senator BUSHBY—But you provide advice to government. In the process of providing advice, did you consider—I am not asking what the advice was—the ANAO’s report on Roads to Recovery?

Mr Ray—Generally movements of funds are principally matters for portfolio agencies and the Department of Finance and Deregulation.

Senator BUSHBY—So once again you just accept what you are told.

Mr Ray—I would not go that far, but there is a division of labour between us and the Department of Finance.

Senator BUSHBY—What are the costs to the Commonwealth of the forgone interest of this \$1½ billion being brought forward a year earlier? In terms of interest.

Mr Ray—We do not estimate those sorts of things.

Senator BUSHBY—But there is a cost. By spending that \$1½ billion a year earlier than otherwise planned, in a debt financing scenario, that means that we have to be able to have a million and a half dollars available to spend a year earlier. Presumably that would come with an interest cost.

Mr Ray—The way that you have framed the question I do not disagree with the concept, but as a general rule we do not separate it all out. It will depend on when in the year. As you know, our financing needs are not just a question of the aggregate, end-of-year budget balance position—

Senator BUSHBY—You have got bonds that are maturing and—

Mr Ray—Yes, and there are the cash flows through the year, and so the question is quite a complex one.

Senator BUSHBY—But on an average basis you could actually look at it and say, ‘We are going to have to increase our financial requirement to cover that this year, and therefore there is an interest cost.’

Senator Sherry—But also presumably, it depends where it is—because it is brought forward from one financial year to another, it does not mean that the actual payment is brought forward for a full year.

Senator BUSHBY—That is right. It is not necessarily 1½ billion times your average bond rate. I acknowledge that. But there is, nonetheless, a cost in terms of interest terms of interest by spending that money earlier than if you had not—

Mr Ray—I agree with that in concept. On the other hand, other spending has been deferred in the budget process. Equally, on the same analysis there would be an interest saving from that.

Senator BUSHBY—What other spending has been deferred? It is a good point. In the context of the reason why I am asking these questions, I am very interested to know whether there has been major spending that was planned and has been pushed out into the coming years.

Mr Ray—I suspect the numbers of movements of funds are in the hundreds. We can take it on notice to find out, but there is a range of spending that has been deferred, including in the capital program for the Department of Defence—

Senator BUSHBY—Deferred with a particular date identified, or deferred indefinitely.

Mr Ray—Deferred with dates identified, including in the water program. There are a number of them, and some are included in the budget.

Senator BUSHBY—Could you give me a complete list of spending that has been deferred together with the amounts and the time lines.

Mr Ray—I will certainly take that on notice. Again, it is one that I am going to send to the Department of Finance.

Senator JOYCE—Without being too pedantic, I want to jump back into your accounting treatment of net debt. What is the current outstanding public service liability?

Mr Ray—For?

Senator JOYCE—It is about \$125 billion or something, isn’t it?

Mr Ray—The superannuation liability?

Senator JOYCE—How much are we actually—

Mr Ray—It is disclosed in the—

Senator JOYCE—Maybe it is \$130 billion now.

Mr Ray—The actual number is probably not in here.

Senator JOYCE—I am trying to do this from memory. It was \$125 billion. It may be up to \$132 billion or something.

Mr Ray—This is an estimate, not an actual. The estimate for the end of 2009-10 is \$123 billion, in round numbers.

Senator JOYCE—How much have we got in the Future Fund?

Mr Ray—I do know that.

Senator JOYCE—Is it \$65 billion or something like that?

Mr Ray—Ms Harris will get it for you.

Ms Harris—As at 30 March 2010 the Future Fund had total assets of \$67.6 billion.

Senator JOYCE—What is our liability?

Mr Ray—It is \$123 billion. That is an estimate.

Senator JOYCE—Where is that \$56 billion liability booked? Seeing that we are putting the assets—

Mr Ray—We book it in net financial worth. I think we have discussed this before. It is precisely for this reason that the government in its medium-term fiscal strategy looks to net financial worth not to net debt.

Senator JOYCE—What is the net financial worth of the government's position in 2012-13?

Mr Ray—In 2012-13 it is negative 11.1 per cent of GDP.

Senator JOYCE—What is that as a number?

Mr Ray—It is \$173.8 billion.

Senator JOYCE—Dollars out the back door.

Mr Ray—I do not want to say 'out of the back door', but negative.

Senator JOYCE—Negative 11 per cent.

Mr Ray—It has been negative for as long as the series has been kept.

Senator Sherry—Including under the previous government, obviously.

Senator JOYCE—How do you define 'booking the asset' in your net debt position when you are not booking the liability in the same process?

Mr Ray—We do not book all of the assets for the Future Fund in net debt. Some of the assets of the Future Fund, the equity fundings and the Telstra holding, are not booked in net debt, and their other alternative assets. Sorry, I take that back. I think alternative assets may be in net debt.

Senator JOYCE—How much is in alternative assets?

Mr Ray—I think \$7 billion.

Senator JOYCE—But they are not in net debt?

Mr Ray—I have to take that on notice because again this is beyond my account expertise. Someone will help me. I have a feeling it might be in net debt but I do not know. But the equity holdings and the Telstra holdings are not in net debt. They are in net financial worth.

Senator JOYCE—So where is the accounting standard that says specifically that you can take up an asset but you do not recognise the eminent liability in the same assessment?

Mr Ray—Senator, if you want to have a detailed conversation about accounting standards you would need to talk to the accountants in the Department of Finance rather than to us.

Senator JOYCE—In my perusal of AASB 1049, I notice that in fact it specifically precludes a corridor approach, so how did you manage to do it?

Senator Sherry—As Mr Ray has already indicated, it is a matter for the Department of Finance.

Senator JOYCE—It calls into question the whole statement of where your net debt is.

Senator Sherry—It is a matter for the Department of Finance, Senator.

Senator JOYCE—In your other building funds, you have booked the asset but you have not booked the fact that we have got the liability out there.

Mr Ray—If the spending occurs in the forward estimates, it has been booked as an expense.

Senator JOYCE—You are saying you have booked it as an expense in your forward estimates but you are booking the asset now against the prospective liability and for an entirely different purpose.

Mr Ray—Everything else being equal, which is always tricky, if we start from a position in which the government is in deficit, there is a corresponding liability, which is the additional debt that has to be erased. It is in the liabilities line.

Senator JOYCE—Basically, to get a full picture and to look at our net debt position now, you have to take into account our future liability position as well for debt in the future.

Mr Ray—I am not quite sure what you mean when you say ‘a full picture.’ I do not think that we or the department of finance or the government would disagree with you that net financial worth is a more complete measure of the strength of a balance sheet than net debt, but in terms of international comparisons net debt tends to be the one that is used because that is the one that is most consistent.

Senator JOYCE—There is a timing issue that comes into play and also the big monster in the room is that the government has underwritten \$57 million of state debt but that is not booked in your net debt position, is it?

Mr Ray—No, but it is reported in the statement of risks because it is a contingent liability which is remote.

Senator JOYCE—If you look at the debt of Japan, does Japan disaggregate the government’s debt and the debt of the other related—

Senator Sherry—If Mr Ray does have some knowledge of the Japanese budget and their fiscal groups, accounting standards and reporting then fine. I suspect he does not. We are happy to take that on notice and get some sort of international comparison with perhaps Canada, which has a federal structure, and Germany. I am not sure about Japan but we are happy to take it on notice.

Mr Ray—Just to try and help: if you look at the sorts of indicators that people who look at these things for a living do—that is, people in financial markets, ratings agencies and international organisations—you can look at gross debt to GDP, net debt to GDP, gross interest to GDP, net interest to GDP and tax to GDP, which gives you an indication of future capacity to raise revenue. You can look at various spreads. No single one of these indicators is necessarily the single thing to look at but, if you look at the whole range of those things, Australia's balance sheet is in pretty good shape.

Senator JOYCE—I don't just want to know it is AASB 1049 because it just says you will comply with the accountancy standards in general. I want to know exactly what accountancy standards you are applying when you say, 'I am applying this and I refer to this accounting standard that allows me to book the asset and not book the liability.'

Mr Ray—As a general rule we apply ABS GFS or AABS 1049. Where those two accounting standards vary and the choice that the government has taken about which one to follow is explained in the budget papers. If you want to ask detailed questions about where this treatment is in the accounting standard, it is better if you ask the department of finance.

Senator JOYCE—But it would be fair to say, without being esoteric, that if someone were to look at it they might say, 'Ah; net debt position means there is a certainty that I will be able to liquidate that asset to pay that debt, because that's how I got a net debt position.' But you cannot go out and liquidate someone else's money, because that money that is sitting in the super fund is not your money. It is the money of the public, it is the money of you people. Unless you want them to pay a debt off with your money, you will not let them do it.

Mr Ray—Net debt is an accounting measure to look at the net debt position of an entity. I agree with you: it is not about whether or not a particular asset is liquid, although in general net debt type assets are more liquid than non-debt type assets such as this building. The issue for lenders, investors, is whether the government has the capacity to meet its obligations and in particular to pay interest at coupon dates. Our gross interest to GDP and our net interest to GDP ratios are very low.

Senator JOYCE—At the moment. How much did you borrow last—

Senator Sherry—Not just at the moment. The forecasts are comparative.

Senator JOYCE—How much gross did we borrow last week?

Mr Ray—It would be—

Senator JOYCE—Well, I know.

Mr Ray—It was about 1.1—

Senator JOYCE—No, it was a little bit more than that.

Mr Ray—It was about \$1½ billion.

Senator JOYCE—Last week?

Mr Ray—Yes. The AOFM are coming tomorrow, and they can tell you the precise figure.

Senator JOYCE—It was in excess of \$2 billion, I think. If you keep going on like that, I do not care what happens: you are going to have a massive problem.

Senator CAMERON—What a joke. You are just a joke in this. No wonder they gave you the flick. You are an absolute joke on this issue.

CHAIR—Senator Joyce has the call.

Senator CAMERON—Your own colleagues do not trust you on it—

CHAIR—Senator Cameron.

Senator CAMERON—Why can't you—

Senator JOYCE—What is the gross debt, Senator Cameron?

CHAIR—Senator Joyce, I suggest—

Senator CAMERON—You are a joke on this.

Senator JOYCE—What is the gross debt?

Senator CAMERON—You got the flick.

Senator JOYCE—You are depriving some poor town of a fool.

Senator CAMERON—You got sacked on this, mate, you were so bad.

CHAIR—Senator Joyce, I suggest, if you do not want to elicit comments, you do not make comments and you continue to ask questions.

Senator JOYCE—Well, control him then, Chair; he is sitting next to you. He is in your party.

CHAIR—We are waiting for Mr Ray—

Senator JOYCE—What is the cost of establishing the Independent Hospital Pricing Authority?

CHAIR—Wait a minute. Mr Ray is still answering your last question.

Senator CAMERON—The Libs controlled you; they sacked you!

Senator JOYCE—Didn't you say he's the piper who calls the tune? That will make *AM*. Another one of your classic comments!

Senator CAMERON—The Libs controlled you. They sacked you, mate.

Senator JOYCE—Another one of your classic comments. You are good for us; you are a big asset for us, Senator Cameron! Don't go anywhere!

Senator Sherry—I notice some of your comments made the news this morning, Senator Joyce. You would not describe them exactly as an asset.

CHAIR—Mr Ray?

Mr Ray—Last week we issued \$1.25 billion of nominal bonds, \$400 million of notes and \$300 million, I think, of indexed bonds—so \$1.95 billion. That is what was issued.

Senator JOYCE—That is a lot closer to \$2 billion than \$1½ billion.

Mr Ray—No, no. I agree. That is fine.

Senator JOYCE—Thank you. What is the cost of establishing the Independent Hospital Pricing Authority under the National Health and Hospitals Network reforms? How many staff will the authority employ?

Mr Ray—Ms Furnell might be able to help you.

Ms Furnell—The Department of Health and Ageing is responsible for the establishment of the independent pricing authority. There are details on the cost in Budget Paper No. 2, on page 233:

The Government will provide \$91.8 million over four years to establish an Independent Hospital Pricing Authority ...

I do not have any details on staffing. I could pass that question to the Department of Health and Ageing.

Senator JOYCE—Budget Paper No. 1 states that, under the state infrastructure fund:

Resource-rich states will receive relatively more funding, reflecting the greater call on their budgets for investment in infrastructure that supports the ongoing development of the resource industry.

Can you provide any more detail on how the fund will be directed to resource-rich states.

Mr Ray—No, Senator. That is subject to negotiations between the government and the states.

Senator JOYCE—So would a resource rich-state include the whole of the state or are we talking about the regions from where the wealth comes from? For instance, if I was to take wealth out of central Queensland, around Emerald, under this fund could you easily say, 'You can now apply that money to Brisbane'?

Mr Ray—I think that is a level of detail that has not yet been concluded. There are clearly options. I think the best answer is that those sorts of details just have not been settled.

Senator Sherry—I am just looking at the announcement and the issue you are going to is not included in the announcement. It says, 'The final details for the infrastructure fund will be negotiated with the states'.

Senator JOYCE—Okay, I will be more precise. There is nothing to say that the money that comes from the regions will go back to the regions, is there?

Mr Ray—Leave aside the question about where the money comes from; the money actually comes from shareholders, many of whom are not even in the country. I think it might depend on need, in part.

Senator JOYCE—Where does it say that?

Mr Ray—It doesn't. But if you were a state government you might be thinking about where is the greatest need—

Senator JOYCE—You might or you will?

Mr Ray—I have never worked for a state government, so I should not guess what they may or may not do. One of the things that the Commonwealth Grants Commission does is to assess needs and in its latest review of needs, one of the things that were changed was its treatment of so-called capital. One of the factors for resource-rich states that also have relatively rapidly growing populations is that their relative need for infrastructure is greater than some of the other jurisdictions. This infrastructure fund supports that.

Senator JOYCE—You said the RSPT is paid by shareholders.

Mr Ray—Yes.

Senator JOYCE—What does that mean for the share prices?

Mr Ray—You discussed this with others.

Senator Sherry—Mr Gallagher outlined that yesterday. I do not know whether you were here or not but he outlined it in some detail. I do not believe we should be going over questions that were answered in detail yesterday.

Senator JOYCE—In the money that has been set aside, the government has said ‘We will collect \$9 billion in royalties and we will pay back \$700 million’. In that \$700 million they pay back, if it is to go to resource-rich states those will include Western Australia and Queensland. But New South Wales has got coal in the Hunter Valley and in northern New South Wales. South Australia has got the uranium but we will see whether they develop it. Even Tasmania—

Senator Sherry—Tassie has got just about everything.

Senator JOYCE—Can you inform me of a state or a territory that is not resource-rich?

Mr Ray—The Australian Capital Territory.

Senator Sherry—Other than the Treasury officials who stay here in estimates—that is a definite resource.

Senator JOYCE—So we can make a commitment tonight that none, or not much, of that \$700 million will be paid in the ACT? Apart of that, what does that statement actually mean—a ‘resource-rich state’? Where in Australia is there not a resource-rich state?

Senator Sherry—As we have indicated, and as I have certainly indicated in the case of Tasmania, the details of this are subject to negotiations.

Senator BUSHBY—Negotiations between who?

Senator Sherry—The states and the Commonwealth.

Senator JOYCE—Let’s go through this. We have got Queensland, New South Wales, Victoria, South Australia, Western Australia, Tasmania and the Northern Territory and they would all be fair to describe as resource-rich states and territories. That is seven. There is \$700 million. That means for all they are paying they are going to get \$100 million a year each if you average it out. How many kilometres of freeway can we build for \$100 million?

Senator Sherry—There has been no suggestion that the money will allocated \$100 million per state. That is your thought-bubble.

Senator JOYCE—It is your statement of—

Senator Sherry—As much as I would like to see money go to Tasmania, for example, I would not under any circumstances expect Tasmania to receive anything like \$100 million, as you are suggesting.

Senator JOYCE—So you have the statement that you pay the superannuation which you do not actually pay, then you have an advance in regional infrastructure which you are not actually going to invest in. The whole thing is a sham.

Senator Sherry—The matter is subject to negotiation with the states. You have referred to superannuation which we do not pay. Again, that is just not correct, Senator. We went through this in great detail last night—the four elements that relate to superannuation in the package and the exact cost to budget. We went through this in detail. You are starting to deliberately waste the time of the committee by going back—

Senator JOYCE—No, Minister, you are doing your weather report tactics.

Senator Sherry—over questions that have been well answered, and they are on the *Hansard* record. Give Senator Bushby a go.

Senator JOYCE—This is the weather report tactic: read out the weather report to waste time. Can you explain the changes—

Senator Sherry—Your questions are much better than Barnaby's.

Senator JOYCE—to the definition of gross national income, which defines the amount of aid we pay under the 0.5 per cent target?

Mr Ray—The short answer is that, when the annual national accounts were released last December, both current and historical GNI were revised up, the current by about \$50 billion, I think. The change came from moving from the old system of national accounts to a new system. I cannot remember the exact reason, so I will take that bit on notice, but it meant that we had a larger base. Absent anything, it would have meant that, if the government maintained its ratios of ODA to GNI, there would have been a sharp increase in the number of dollars of aid, just as a result of this definitional change, so the government decided to phase in the effect of this change in the denominator on the numerator.

Senator JOYCE—Just going back to the resource super profits tax, doesn't the RSPT share characteristics with bonds—that is, isn't the government taking extra risks such as a downturn, where it will be liable for a payment? Where it is liable for payment, will those risks be recognised in the budget papers?

Mr Ray—Everything else being equal, I think it is a reasonable statement to say that the move to an RSPT introduces additional volatility into the Commonwealth government's revenue base. The way that that has been accounted for is that it is taken above the line in the revenue estimates so that the estimate of potential losses has been included in the revenue estimate line. In the statement of risks, which is statement No. 8, there is a general statement about how revenue is subject to movements in the economy, and I think it specifically mentions the RSPT in relation to commodity price movements et cetera.

Senator JOYCE—Going back to our accountancy standards, that is a substantial risk you are taking on. You have said that if the mining projects in Australia go bad we are up for 40 per cent of the costs. Surely that is worth at least a note in its own right at the end of the

accounts. If you presented a company with a set of books and they said, 'Is there anything here we should know about,' and you said, 'We've picked up 40 per cent of the losses of all the mines in Australia but we've just contra'd it out in the income,' the partner would drag you screaming across the floor and say, 'You'd better have some working papers up here on that in the next 24 hours or we will not be issuing any sort of audit report on these books.'

Mr Ray—I do not know about that, but the approach we have taken is to quantify the estimate and to include that in the revenue estimates. Rather than say that there is a possibility that this will happen, we have estimated that possibility and included it in the account.

Senator JOYCE—I am sure someone is out there, a board accountant who is half finishing work and getting into lodgements and trying to polish things off, who would be absolutely fascinated to know that in our nation's books we have taken up 40 per cent off the liability of the mining sector yet we cannot direct you to a note to express what that amount is, nor can we direct you to a note to tell you how we netted it out.

Mr Ray—I am not sure there is a question in there.

Senator JOYCE—The question is yes or no. There is no note, no working paper, no discernible thing I can pick up in the budget papers and say, 'Ah, they are presuming a net liability of X amount of projects that go bad; there's a total potential liability of X, a probability of Y, a booked amount of Y by X, and this is what is in the books.'

Mr Ray—The revenue estimates incorporate an estimate of what you are talking about, and then in statement 8, statement of risks, the variability that comes with the resource super profits tax is expressly mentioned. I do not know that it is in a note but it is in the statement of risks.

Senator JOYCE—We guaranteed the banks. What was the total potential liability of what we guaranteed—it was about \$850 billion or something, wasn't it?

Mr Ray—Are you talking about the guarantee of large deposits and wholesale funding?

Senator JOYCE—Yes.

Mr Ray—As at 5 April 2010, total liabilities covered by the guarantee were estimated at \$169.6 billion.

Senator JOYCE—That is all right; I have got that—\$169.6 billion potential. We know that is not going to happen. It is highly unlikely but it is there. We have got it; we have got the working papers behind it. Okay. What is our potential liability to the mining sector?

Mr Ray—I think that is a slightly different question. This is a potential liability. The wholesale funding guarantee is a contingent liability which is both remote and unquantifiable. The other liability that—

Senator JOYCE—Did you say that the mining liability is remote and unquantifiable?

Mr Ray—No, the one for the wholesale funding guarantee.

Senator JOYCE—But we managed to get a number for that.

Mr Ray—No, we have not. In fact, we have had discussions about that in the past. The contingent liability is remote and unquantifiable. That number is the total amount covered by the guarantee.

Senator JOYCE—Okay, but you would disseminate that amount from—I know because the numbers have been run past us before. You did actually have the total amount of what the bank guarantee covered. There was something like \$850 billion and then it broke—

Mr Ray—I think that is the deposit one. For the purposes of this conversation—

Senator JOYCE—You know the question I am getting to: why can we do it for the bank industry yet we could not do it for the mining industry?

Mr Ray—Yes. I know where you are going. In the case of the financial claims scheme and the wholesale funding guarantee, they are contingent liabilities that are remote and unquantifiable. We have not quantified the liability. What we included in the statement of risks is an estimate of which deposits are eligible for the guarantee and those sorts of things, so it is a different thing. In the case of the resource super profits tax, the revenue estimate includes all the elements of the tax, including the matter you are going to, so it is incorporated in the revenue line; it is quantified.

Senator JOYCE—Why can we not pull out that amount and say: ‘This is how we came to that \$9 billion figure. We’re going to pay out this amount for all these projects that go bad’?

Mr Ray—That is a question you will need to direct to my Revenue Group colleagues. If you want to know how the estimate is built up, they can provide you with more information.

Senator JOYCE—Have you run some scenarios about what will happen under different assumptions of different mining sector performances?

Mr Ray—One of the scenarios in the sensitivity analysis, which is incorporated in the budget, is what would happen to the budget estimates if the commodity prices were lower. As to the specific thing around just looking at the mining sector, I do not know whether we have done that.

Senator JOYCE—I am sorry; can you repeat that Mr Ray.

Mr Ray—In the sensitivity analysis, which is in appendix A to statement 3, a scenario is run which is just illustrative. It is called the ‘Illustrative impact of a permanent non-rural commodity price fall consistent with a 1 per cent fall in nominal GDP in 2011-12 (per cent deviation from the baseline level)’. There is another one entitled ‘Illustrative sensitivity of the budget balance to a 1 per cent decrease in nominal GDP due to a fall in the terms of trade’.

Senator JOYCE—What page are you on?

Mr Ray—We are on pages 3-24 and 3-25.

Senator JOYCE—Which budget paper?

Mr Ray—It is in Budget Paper No. 1. So the specific thing we look at is the illustrative impact on the budget of a permanent fall in world prices of non-rural commodity exports.

Senator JOYCE—Where is the money in there that we are actually paying out to projects that go bad? That is not in there. That just talks to the revenues, doesn’t it?

Mr Ray—It is a more general thing, so the measure that is included in the budget would be a central estimate.

Senator JOYCE—What does ‘central estimate’ mean?

Mr Ray—There is no sensitivity around the individual measure.

Senator JOYCE—There is no sensitivity around it?

Mr Ray—Not published in the budget.

Senator JOYCE—Not published in the budget?

Mr Ray—Yes. Whether my colleagues in the Revenue Group have looked at sensitivity analysis, I do not know; you would need to ask them.

Senator JOYCE—For risk management purposes, would it not be more diligent to have greater sensitivity to the risk management?

Mr Ray—Are you saying: could we include additional scenarios, or could the government include additional scenarios and have further sensitivity analysis in the budget? I suppose it could.

Senator JOYCE—This is a substantial income stream. It is a massive income stream and a substantial risk.

Mr Ray—Again this is not quite in the right group, but I think if we went back and looked at the impact on capital gains tax receipts of developments in 2008-09, you would see that they were pretty significant and substantial too.

Senator JOYCE—The capital gains tax?

Mr Ray—Yes, or tax receipts generally on what happened in the economy.

Senator JOYCE—But we did not pick up a contingent liability with the introduction of the capital gains tax. We never said to people, ‘If you lose money you’ll have a capital loss, but we don’t actually have to pay you out the money.’ In this one, we actually have to send them a cheque in the mail for the loss.

Mr Ray—True, but if you get a capital loss you carry it forward.

Senator JOYCE—Yes, but this is entirely different. A capital loss is only carried forward to the point in time where you have a capital gain and you then write one off against the other. The government never actually has to send out a cheque. In this case, my oath, they are sending you a cheque for billions of dollars in the mail.

Senator Sherry—Putting aside the rhetoric and the other language—

Senator JOYCE—The other language?

Senator Sherry—The question, to the extent there was a question there, was surrounded by substantial rhetoric, political argument et cetera, which Mr Ray, to be fair, cannot go to. You touched on, referred to, probed and questioned on this issue with the Revenue Group, which is the appropriate group. You are perfectly entitled to come back and try a second time around, but—

Senator JOYCE—To get answers for the Australian people? Is that what I am trying to do?

Senator Sherry—This is not the appropriate area of Treasury.

Senator JOYCE—So that is the weather for today. That is two minutes of our lives we will never get back. I have been looking at an ad that you have had in the paper. You are seeking a suitably qualified and experienced speechwriter—I would like to suggest Senator Cameron—to prepare engaging and influential speeches to be delivered by the Treasurer, other Treasury portfolio ministers and senior Treasury staff. I notice that you are paying them more than we get paid.

CHAIR—That is because they are going to be engaging.

Senator JOYCE—Can you please explain to me what an engaging speech is?

Senator CAMERON—The one you gave at the Press Club. Remember the one before you got sacked?

Senator JOYCE—Can you give me an example of an engaging and influential speech, as opposed to a boring and pointless speech?

Senator CAMERON—The one you gave at the Press Club. Remember that one?

CHAIR—Order! I think we are all interested in this question.

Senator JOYCE—\$157,505 per annum is not a bad wicket. Has that job been filled?

Mr Ray—I have a feeling it may have been.

Senator JOYCE—Who is the lucky soul who got that?

Mr Ray—That is a question I do not know the answer to.

Senator JOYCE—What speeches have they written lately?

Mr Ray—I do not know that the person has started.

Senator BRANDIS—We will know when they have started when we start hearing engaging speeches.

Senator JOYCE—Can you direct us to when you think we might be seeing the first work from this bard of the Treasury?

Mr Ray—I am happy to take on notice when we expect this person to start work.

Senator BRANDIS—This Cicero!

Senator JOYCE—This Tennyson of tax!

Senator Sherry—Very good.

CHAIR—Perhaps you should apply for the job, Senator Joyce.

Senator JOYCE—It is not a bad wicket.

Senator BUSHBY—You would get a decent pay rise out of it.

Senator CAMERON—Accountants are not allowed.

Senator JOYCE—I have some questions on funds allocated in the Department of Climate Change and Energy Efficiency budget. Have we dealt with the \$132 million that was allocated to a program that no longer exists?

CHAIR—Yes.

Senator Sherry—We have had questions on that.

Senator JOYCE—Are you aware of a company Serco Pty Ltd?

Mr Ray—No.

Senator BUSHBY—They should be.

Senator JOYCE—You should be.

CHAIR—Would you care to elucidate?

Senator JOYCE—There is a company called Serco Pty Ltd. Has the department agreed to limit this company under contracts that were signed in December last year?

Mr Ray—I honestly do not know what you are talking about, so I will take the question on notice and find out.

Senator JOYCE—How about if I give you a bit more information?

CHAIR—I think we might be pretty close to the dinner break, so I will suspend this hearing. I thank the Fiscal Group of Treasury for coming along to estimates.

Proceedings suspended from 5.29 pm to 6.31 pm

Australian Competition and Consumer Commission

CHAIR—Welcome. Mr Samuel, I understand you have an opening statement you would like to make.

Mr Samuel—I do. I do not want to take up too much time with this—Senators do have questions. We have a fair amount of time allotted to us. I am anxious to put two or three significant matters on the record, but I suggest that if senators are getting a bit concerned about the time being taken up you should signal to me. I will endeavour to cut short. There are some matters that I do want to mention specifically. The topics I want to try to cover tonight if I have time relate to mergers, tougher sanctions for anticompetitive conduct, cartels and criminal penalties, some of our enforcement actions particularly in the area of small business which have proven to be very significant and quite interesting over recent times and work we are doing in product safety which is proving to be a significant move forward. This may help some of the senators with some of the issues that I know they have raised on previous occasions.

The merger process is working very well at the moment. As senators would be aware, we have a refined informal process which was set in place in 2004. It is a flexible process that allows us to be responsive to individual transactions and circumstances and, at the same time, to be sure that we can achieve maximum transparency but not compromise the fundamental principles of our processes: protection of confidential information, timeliness and fairness of review processes and, most importantly, getting the right answer, which is important because if we get the wrong answer in respect of a merger it is almost impossible to undo the position.

In the past financial year up to 1 June, we have conducted 274 merger assessments, including 147 reviews. To give you a bit of a sense of the statistics, there are 274 total matters that have been examined, 256 that were not opposed, four that were cleared with undertakings—competition concerns have been dealt with—and 14 that were opposed or had concerns that were expressed confidentially.

I should emphasise the context of matters that were opposed or dealt with confidentially, because what does not often appear publicly is that there are a number of mergers where we will oppose them confidentially. They will never hit the public eye. That leaves aside the fact that there are also a large number of mergers in which we get some information that suggests that they were being contemplated by the parties but they had taken the view that it was not even worth proceeding, because they considered that the ACCC would inevitably oppose the transaction; therefore, they did not even get to the point of being referred to us.

Other mergers are actually never referred to us as I have mentioned—some of those are dealt with confidentially. I think it is probably fair to say that there is a far more significant percentage of mergers that are actually not proceeding because of the operations of section 50 of the Trade Practices Act that might otherwise appear to be the case if you look at the basic statistics.

The time lines for dealing with mergers have been fairly strictly maintained since we put in place the process guidelines in 2004. I am pleased to be able to say that between 87 and 92 per cent of mergers or merger reviews are conducted within about eight weeks, which is probably—I think I can say without fear of contradiction—international best practice. Some of the other major jurisdictions—the EU, UK, US—can take sometimes four or five months and in some cases, particularly the UK, they have up to about 24 weeks for the competition commission to assess mergers. Our team manages to do them in about eight weeks except where they become very, very complex issues and then they may well take longer.

You would be aware of some of the mergers that have been currently either opposed or, in one case, still in play. NAB-AXA of course has been initially opposed by us but it is still in play—I think is the best way to describe it and I will not make any more comments on that. We opposed the Caltex acquisition of the Mobil retail assets. You will be aware that of more recent times it has been announced that the 7-Eleven group, with the exception of South Australia, will acquire those Mobile retail assets, and Peregrine will be acquiring the retail assets of Mobil in South Australia. Those acquisitions are themselves still subject to appropriate merger review, and so at this point in time have not been cleared in accordance with section 50 of the Trade Practices Act. We oppose the Link acquisition of Newreg, which was in the share registry business; Thomson Reuters acquisition of some Ernst & Young software business; Cargill and the Goodman Fielder assets in relation to fats and the like; and GUD-Breville. So there a number of mergers that we have opposed.

There is some suggestion in public commentary that this is a new practice on the part of the ACCC or a more rigorous approach being adopted. I can absolutely assure you it is not. We are operating out of the same section 50 of the act with the same considerations and the same rigorous analysis. It just happens to be that we have had some rather complex and difficult mergers that have come to us in more recent times which have led to some opposition. I think it is also fair to say that our record in opposing mergers certainly over the past six or seven

years has been remarkably successful in the sense that only in one case, which was back in 2003—AGL-Loyang—were we overturned in the Federal Court. In every other case where we have opposed a merger, it either has not proceeded or it has gone to court, and in one case it was dealt with with appropriate section 87B undertakings.

I want to move to tougher sanctions. This is a very important area for us now in the context of the amendments to the Trade Practices Act that were introduced and came into force on 1 January 2007. I think it is appropriate to refer the committee's attention to these amendments, because they are now starting to have an impact in relation to our enforcement activities. The committee will be aware that for roughly 14 years the maximum penalty for anticompetitive conduct, be it misuse of market power or cartel conduct, was \$10 million per contravention. Parliament passed and brought into play as from 1 January 2007 new penalties which provided that the penalty regime for any anticompetitive conduct, be it cartels or otherwise, would be the maximum of \$10,000; or three times the value of the benefit that one or more persons obtained from the anticompetitive conduct or, where the value cannot be determined, 10 per cent of the annual turnover of the company and its related companies—that is, of the whole corporate group—during the period of 12 months ending at the end of the month in which the conduct occurred. In addition, the civil penalties include the ability for the court to disqualify a person who has been involved in the anticompetitive conduct from managing corporations for such a period as the court thinks fit. There is no limit on that other than life.

I have to say we are now entering a new era. For some time we have been concerned that the penalties available in Australia for anticompetitive conduct have simply made a quite interesting business case for those engaged in that conduct—that is, if I engage in the conduct then I will pay a fine; the fine will be a mere fraction of the profit derived from the engaging in the conduct; therefore, it is a pretty good business deal to do so knowing that the financial penalty will not be anywhere near the benefit that I have obtained from engaging in the anticompetitive conduct.

That will change in respect of all conduct that has taken place after January 2007, and there are now matters on our books that fall within that scope. We will be requiring parties or businesses that have engaged in conduct that might be subject to the new penalty regime to open their books. We will be using our investigative powers and, potentially, engaging forensic accountants to obtain information from firms and establish the benefit gained from the anticompetitive conduct. Then the submissions made to the courts will seek the greater of \$10 million and three times the gain as established by that forensic analysis, or 10 per cent of turnover if it is not possible to establish the gain. That really suggests to business that it is not longer a sensible business plan to engage in anticompetitive conduct, be it cartels or whatever, and to believe that you can make a profit out of it, because if we do seek three times the gain that will be a very substantial penalty indeed. That brings us into line with other significant antitrust regimes, particularly the US, the EU, Canada and Japan, by focusing on the impact of the conduct to calculate penalties and to determine the appropriate sanctions.

If that is not enough to deter people, then, in relation to cartels, we now have the criminal provisions that were introduced as from July last year. In the context of cartels, we have had a record year in calendar 2009. We instituted proceedings in 13 cartel matters and obtained penalty orders totalling over \$20 million in a number of cases, which I can quickly detail:

April International Marketing Services, the Australian Karting Association, Martinair Holland, Cargolux Airlines, and Societe Air France and KLM. As a result of our continuing and continued investigation into alleged fuel surcharge price fixing in the airline industry, to date the Federal Court has ordered a total of \$41 million in penalties against respondent airlines. On 11 December 2008, which was the first of them, Qantas and British Airways were required to pay penalties of \$20 million and \$5 million respectively. On 16 February 2009, Societe Air France, KLM, Martinair Holland and Cargolux were ordered to pay penalties of \$3 million, \$3 million, \$5 million and \$5 million respectively. So the penalties are reasonably significant, but, of course, they also have to be seen in the international context. There have been penalties also levied in other jurisdictions where that international fuel surcharge price fixing was operating. We have instituted proceedings in the Federal Court against Singapore Airlines, Cathay Pacific, Emirates, PT Garuda Indonesia, Thai Airways, Korean Air Lines, Malaysia Airlines, Air New Zealand and Japan Airlines. So a range of matters are occurring in relation to that, and that is a very significant cartel matter for us. Other recent cartel outcomes include the marine hose cartel, where four foreign based suppliers of marine hoses were ordered to pay penalties of \$8.24 million for cartel conduct. That cartel submitted rigged bids to supply marine hoses to customers in Australia.

Both the marine hose and, as I mentioned before, the air cargo cartel cases demonstrated in a very tangible manner the outcomes that can be achieved through international engagement and the cooperation that we were able to engage in with our counterparts overseas. The marine hose cartel investigation and prosecution would not have been possible without extensive cooperation with authorities in the United Kingdom and the United States, including the provision of evidentiary material that had been gathered in the UK investigation. So the context of international cooperation has been very important indeed.

An important cartel prosecution concluded just recently, in April this year, involving Admiral air conditioning and others. This involved 17 companies and 22 individuals involved in collusive tendering for air-conditioning contracts for schools, hospitals and shopping centres in Western Australia. In total, pecuniary penalties of \$9.271 million were imposed on respondents in these proceedings. They were very extensive indeed in terms of the operation of the cartel. We calculated that air-conditioning projects totalling about \$129 million were involved in that particular cartel.

I mentioned the civil sanctions that are available for anticompetitive conduct before. That applies to cartels. Importantly we now have the criminal provisions. All cartel conduct, entering into or giving effect to a cartel, post 24 July 2009 is being treated as a potential criminal prosecution and is initially investigated under the criminal investigation process, with a potential penalty of up to 10 years jail for any individuals involved.

There have been a number of matters that have come before us having a post July 2009 element. At a point in time we make a decision as to whether the criminal investigation should be relegated to a civil investigation. We do that in the context of the memorandum of understanding with the Commonwealth Director of Public Prosecutions—which is public; it is on our website—and that is, essentially, if the matter is not considered to be a serious cartel or, after consulting with the CDPP, taking into account the criteria set by him under the Commonwealth's prosecution policy.

I want to make absolutely clear some issues in relation to the ACCC's position on plea bargaining. We have an inflexible position that a criminal cartel prosecution is not negotiable. Cartel participants will not be able to buy their way out of a criminal conviction and jail. We will not put ourselves in a position where there might be a perception that we are using the possibility of a referral of a matter for consideration of a criminal prosecution to obtain cooperation or resolution of civil proceedings. We will not engage in discussions with parties under criminal investigation as to the possibility of a civil resolution—that is, of a financial penalty—unless and until we have formed the view, totally independently, that the matter is not appropriate for criminal prosecution because of the operation of the memorandum of understanding I referred to before or the Commonwealth prosecution policy. We will not even discuss the proposition.

If a party comes to us and says: 'We understand that we are being criminally investigated with a view to a criminal prosecution. Is there a way that we can pay a significant penalty—that is, a financial penalty—to avoid the prospect of a jail sentence?' our investigators are instructed at that point to walk out of the room. They will not negotiate. If we commence a criminal investigation and continue it because it fits within both the memorandum of understanding and the Commonwealth prosecution policy and the CDPP determines to criminally prosecute, then it is in his hands; we will not negotiate away from that criminal prosecution. A way of summarising it is this. In the case of serious cartel activity, no matter how fat the cheque book or to what lengths a corporation will go to defend the position of its executives, there is no amount of money that will remove the risk of the executives implicated going to jail.

The next subject I want to cover is small business. As we are well aware and has been established by a committee of the Senate in a report delivered in 2004, the fundamental philosophy underpinning the Trade Practices Act is the promotion of competition, not the protection of competitors or any sector of the economy from competition. We are all aware that there are a number of protections available to small business, with differing degrees of success. There are codes of conduct—the Franchising Code, the Horticulture Code. There are the unconscionable conduct prohibitions—that is, small operators dealing with big customers or suppliers. There is section 46 on misuse of market power, including 46(1AA), the so-called Birdsville amendment, which relates to predatory pricing. Also, small business can help itself through collective bargaining. We have adopted a series of highly facilitative practices and processes within the commission to facilitate the collective bargaining process, with appropriate limitations, particularly in relation to collective boycotts.

It is appropriate to mention a couple of matters that have recently been dealt with within the litigation process by the ACCC. On one of them, judgment was handed down just two or three days ago. This is the Seal-A-Fridge matter, where the Federal Court found that a franchisor, Seal-A-Fridge, engaged in unconscionable conduct by unilaterally imposing fee increases on its franchisees for use of the Seal-A-Fridge national phone number. The phone number is used by franchisees to receive customer inquiries and work. Seal-A-Fridge used the tactic of disconnecting franchisees from the phone number to procure agreement to pay the increased fees. The court also found that Seal-A-Fridge breached the Franchising Code of Conduct by failing to provide adequate disclosure to a franchisee prior to them entering into

the franchise agreement and by failing to provide current disclosure documents to franchisees after receiving written requests.

This is part of the process that we pursued two or three years ago—and I said publicly that we would do so—to try and test the limits of the unconscionable conduct provisions, which are very important indeed in dealing with some of these franchise issues and issues relating to small business. The Federal Court found that Seal-A-Fridge's behaviour surrounding attempts by franchisees to transfer their franchises was not unconscionable but that the other matters that I have referred to were unconscionable conduct, and appropriate orders were made. This was important in enabling us to establish a bit more clearly what is the role of the unconscionable conduct provisions under the Trade Practices Act and to deal with the issue of the Franchising Code of Conduct.

The Allphones case received a fair degree of publicity. It was determined in April 2010. We alleged that Allphones engaged in unconscionable conduct by failing to disclose or pay certain income to franchisees, implementing policies targeting certain classes of franchisees and threatening or engaging in a pattern of harsh conduct against franchisees. We also allege that Allphones failed to comply with the franchising code and engaged in misleading or deceptive conduct towards franchisees. The Federal Court declared that Allphones engaged in misleading and deceptive conduct, contrary to the franchising code, and also engaged in unconscionable conduct. So all three areas were covered.

The court ordered a number of injunctions, but, most importantly in the context of this case, we took action to see if we could recover some damages to provide some assistance to franchisees that had suffered damage at the hand of Allphones. We recovered on their behalf in effect \$3 million of damages. That \$3 million will be divided amongst the franchisees represented by the ACCC according to the time frame that they were a franchisee and the duration and performance of their business. It reflects an underpayment of rebates and commissions and the implementation of charges by Allphones. I have to say that this was a case of sustained and systemic unconscionable conduct and one of the worst cases in the franchising system that we have ever encountered in the ACCC.

There have been other matters, which I will not go into because time will not permit. An example is Australialink Pty Ltd, where consent orders were obtained for misleading, deceptive and unconscionable conduct in breach of section 52 and 51AC of the Trade Practices Act. Then there was the Dukemaster case, which I think we may have already mentioned, where a landlord in a shopping centre in Melbourne engaged in unconscionable conduct by exerting undue pressure and using unfair tactics against four tenants in connection with their leases in that shopping centre.

Separate from the litigation process, we have announced today that we have sponsored a franchising education program, which is being done in conjunction with Griffith University. It is to establish a one-stop shop for education programs for people buying a franchise. It provides potential franchisees with a better understanding of their rights and obligations under the franchising code and some of the practical issues they could face as a franchisee. A link to that is available on our website.

There are just two more items I want to mention. In the area of enforcement we have had one or two interesting cases, one of which will interest Senator Xenophon, who is here. That is the Heinz Golden Circle matter, where they had, in misleading and deceptive conduct, engaged in labelling their products as being Australian owned when in fact they were not, given that Golden Circle were taken over a year earlier by the American Heinz group. There is \$1.8 million worth of canned fruit that is to be removed and distributed to charities, through a company called Foodlink. We are aware that there is still some product on the shelves. In the past couple of days we have communicated with the Golden Circle to seek a speedy removal of that food from the shelves, pursuant to the undertaking that has been given to us. We will come to that, I am sure.

Senator XENOPHON—Chair, could Mr Samuel provide a copy of his opening statement to us? That might be useful.

Mr Samuel—Yes, I will do that. If it is permissible, I will give you the total statement.

CHAIR—Certainly.

Mr Samuel—The final thing I will mention very briefly is that in the area of communications we have undertaken a number of global solutions, if you like, to some issues. I mentioned last time the global solution we adopted in respect of advertising, which has not, by the way, stopped some of the enforcement activities that we are undertaking in relation to advertising practices where we do not believe the appropriate standards are being met under the Trade Practices Act. But in addition, we have secured from Vodafone Hutchison a section 87B undertaking—that was in January this year—in relation to the rights of consumers who purchase a phone in conjunction with a service contract which may last, say, for two years, but the phone ceases to operate, becomes faulty, in the course of that service contract. We are currently talking to Telstra and Optus about the same issue, fundamentally saying that if they sell a phone, at the same time belting it up with a service contract for two years, consumers ought to be able to expect that the phone will operate for two years and that they will repair it if it does not. So we have dealt with that. I will call a halt at that, but I will table some of these comments, if that is appropriate, Chair.

CHAIR—Yes, you can table them.

Senator IAN MACDONALD—I thank my colleagues for allowing me to interpose very briefly. That is very useful information for the committee in the future, but it would certainly help if the committee got that a day before and it were incorporated, because time is precious here and we really do begrudge giving of our time to question you with those long statements. Perhaps in the future that very useful information can be made available—

Mr Samuel—I will take that—

Senator IAN MACDONALD—and incorporated into *Hansard* as well. In the February estimates I did raise with you the issue of Mercedes-Benz Australia/Pacific—and I had written to you about it. I am conscious that Minister Emerson on 3 March indicated that he was having the most sweeping reform of the Franchising Code of Conduct since its inception 12 years ago. In asking my question, I just draw your attention to this case that I have been following where a dealer drew to the attention of Mercedes-Benz to their possible breach of competition policy in Australia. Not long after that the dealer lost the dealership and there

were a lot of allegations made which have proved to be incorrect. My question is: are you aware that Mercedes-Benz in the United States has recently settled at US\$184 million and has entered into a Department of Justice agreement on a deferred prosecution in relation to similar activities—this is by Daimler, who, I understand, own Mercedes-Benz Australia. Daimler's violations in the United States were relating to similar things that appear to be a course of conduct here in Australia and, as part of that settlement in the United States, they agreed to implement compliance and ethics programs.

By the same token, I just mention that today I have been advised that two large New South Wales dealers are being non-renewed—by a different maker, not by Daimler Mercedes, but using the precedent of Mercedes-Benz in what they have been doing over recent months to the dealers. My question to you really is: where have you got with your investigation into what Mercedes-Benz has been doing in the case I have related to you—and I do not want particularly to mention names here? Has the investigation gone any further? Are you perhaps in a position to relook at your investigation into Mercedes-Benz following these United States' cases?

Mr Samuel—Senator, as you will be aware, it is not our practice to comment publicly on matters that we may or may not be investigating so I am constrained that we cannot actually give you some information on that particular matter. Mr Ridgeway, do you want to add anything to that given that we cannot comment?

Mr Ridgeway—There is not much I think I can add.

Mr Samuel—I think the answer is no.

Senator IAN MACDONALD—Don't comment on the specifics, but you are currently investigating those types of matters—though not necessarily this matter and those people—in that sort of area of your interest.

Mr Samuel—I think it is fair to say that there are a number of franchising issues that we are investigating. I do not want to identify the sectors or the like but want to say that franchising is very much on our radar. I think I have illustrated my very, very rapid coverage of that area, and there are some more materials in the statement. There are a number of cases that we have taken. As I have indicated, there are three heads involved in pursuing franchising matters. The first is breaches of the Franchising Code of Conduct. The second is the issue of misleading and deceptive conduct. The third is unconscionable conduct.

The unconscionable conduct area is somewhat more difficult to investigate because it involves parties who may have been subjected to intimidatory tactics and the like having to give evidence to us that can then be put before a court, which in its own sense is not a comfortable environment for those who have been subjected to harsh and oppressive or intimidatory tactics. It is not a friendly environment for them to be involved in. It is not an easy area, but I have to say to you that we have taken a decision that we want to try and pursue the issue of unconscionable conduct a little more vigorously than perhaps might have been the case in the past, not least because now it is possible for us to obtain financial penalties for breaches of those provisions.

Senator IAN MACDONALD—Do you follow things that happen in other countries with perhaps a view to watching what international companies do in Australia as well?

Mr Samuel—We follow closely what is occurring in other countries. We have a strong cooperative liaison, particularly with the United States, the United Kingdom and Europe. I think it is fair to say that often matters will arise there that will spark an interest at the Australian end which will cause us then to check and investigate whether in fact there may be similar policies being followed by related companies at the Australian end. Yes, that has been of great value to us.

Senator IAN MACDONALD—Thank you very much for that, Mr Samuel, and again thanks to my colleagues for allowing me to interpose.

Senator JOYCE—I am a betting man, so I am going to lay a bet that you can guess what the first question I am going to ask is about.

Mr Samuel—Yes, Senator. Do you know what? Because Mr Cassidy and I have answered this question so often in the past and clearly have not been able to satisfy you with our answers, we have decided to delegate the answering of this question to Mr Bezzi, who is going to answer it. Do you want to provide the answer before the question is asked?

Senator JOYCE—What would I ask? What would I open up questions with? I am a betting man. I know we are not going to meet a billion-dollar surplus. I will put a thousand bucks on the table if they can tell me the first question I am going to ask about. Mr Bezzi, what am I going to ask a question about?

Mr Bezzi—How many Birdsville related complaints—

Senator JOYCE—There you go!

Mr Samuel—Do we get the thousand dollars, Chair, or not?

Senator JOYCE—My first question is: how many complaints have been received regarding possible breaches of the Birdsville amendment? Fire away, Mr Bezzi.

Mr Bezzi—At our appearance on 10 February we outlined that between 18 September 2007 and 31 December 2009 the ACCC had received 378 contacts relating to predatory pricing, comprising 349 alleging predatory pricing and 29 seeking information about the provision. As of 30 April 2010 the ACCC had received 426 contacts relating to predatory pricing, comprising 392 alleging predatory pricing and 34 seeking information about the provision. That is an increase of 48 contacts in total, comprising 43 alleging predatory pricing and five seeking information about the provision.

Senator JOYCE—Well, it seems to be working. The public seem to be aware of it, which is good. Can the commission indicate how many Birdsville amendment related cases have been subject to a full investigation since the last estimates?

Mr Bezzi—A total of 77 matters of alleged predatory pricing have progressed to the initial investigation stage, representing just over 18 per cent of the contacts. This is, I should say, significantly higher than the average for part IV complaints progressed to initial investigation, which is about 11 per cent. Of the complaints received since our last appearance, three have progressed to an in-depth investigation stage, and we currently have three active predatory-pricing investigations. As I think we have advised in the past, we have also instituted proceedings against Cabcharge, alleging predatory pricing, amongst other things, although the allegations relate to the period before the introduction of section 46(1AA).

Senator JOYCE—The Birdsville amendment.

Mr Bezzi—Yes.

Senator JOYCE—You have commenced legal proceedings on Birdsville amendment cases or you have not?

Mr Bezzi—No, not yet. We have three matters which may end up going that way. We are not able to say yet. The investigations are continuing.

Senator JOYCE—Obviously we are very interested, and have been for a number of years now, to see the jurisprudence associated with Birdsville amendment cases come to light. I think the only way it will ever happen is if a case is taken into the courts.

Mr Samuel—As I think we said at the February estimates, you would be well aware that under the Legal Services Direction we cannot commence proceedings in relation to a matter unless we can receive legal advice that we have a reasonable basis, reasonable grounds, for instituting proceedings. I think that, in answer to questions that were put to us by Senator Brandis at the last Senate estimates, I made it absolutely clear that there has been no matter where we have received legal advice to say that proceedings could be instituted where we have taken a decision not to institute proceedings. So there has not been any arbitrary decision not to institute proceedings, but if the legal advice does not get us over the hurdle of reasonable grounds it is not appropriate under the Legal Services Direction for us to commence proceedings. I would not want to concede this to you too quickly, but it just may well be that the very existence of Birdsville and some of the uncertainty as to what it actually does mean may be deterring parties from engaging in conduct that might otherwise breach section 46(1AA), so you might have achieved your objective.

Senator JOYCE—I will take that as a win.

Mr Samuel—I did say that I would not want to concede that to you too quickly, Senator, but that is all right.

Senator JOYCE—I think as I leave here they will talk about a whole range of things. Someone asked me, ‘What is your biggest achievement?’ and they were expecting me to say the ETS. I said, ‘The Birdsville amendment,’ and they said, ‘What the hell’s that?’ Isn’t it a case of us chasing our tails? Unless we get a case to court, we are not going to dispel all this conjecture about the interpretation of the Birdsville amendment.

Mr Samuel—You say that, Senator, but it just may be that the existence of Birdsville and the uncertainty associated with it are leading businesses to being far more cautious against what some might interpret as being predatory pricing. That is to concede to you that it might be having the sort of effect that you and others who promoted the Birdsville amendment sought to achieve. We will not go into some of the discussion about what else section 46 might otherwise have achieved in any event because it does not matter; it is now part of the law. Suffice it to say this: as I have said on previous occasions, Birdsville type cases are being investigated. Where there is any prospect of the matter being referred to court then it is subjected to legal analysis, but we are yet have a case before us where the legal analysis has indicated that we have reasonable grounds for instituting proceedings—keeping in mind, by the way, that that legal analysis will, of necessity, say that there are some questions still to be

answered about what ‘selling below relevant cost’ is, what ‘a substantial share of the market’ is and what ‘a sustained period’ is. Given that there are question marks about the meaning of those, if it is in doubt, at least the legal analysis would entitle us, with the appropriate legal advice, to assume that there might be reasonable grounds for instituting proceedings, if only to test the interpretation of those provisions. So I think you can be satisfied that, where investigations have taken place and have been referred to legal counsel, legal counsel has said that on any analysis, on any interpretation, of those tests and, as well, the purpose test—that is, the fourth limb of section 46(1AA)—there are not reasonable grounds for instituting proceedings. The Legal Services Direction says that we, like any other agency, cannot in those circumstances institute proceedings.

Senator JOYCE—I am confident. And, obviously, it gives us all—because it is not just me; it is Senator Xenophon, and a whole range of other people who are engaged with the Birdsville amendment—the sense that if it is having an effect and mollifying the actions that in the past have been obnoxious then that is a good thing. So the commission has not commenced any legal proceedings in any Birdsville amendment related case since the last estimates—you have basically confirmed that, haven’t you?

Mr Samuel—That is correct.

Senator JOYCE—So is the ACCC any closer to issuing any guidelines on the interpretation of the Birdsville amendment?

Mr Samuel—I think I will refer this to Mr Bezzi as well, because neither Mr Cassidy nor I can give a satisfactory answer on this one.

Mr Cassidy—Our answer has not changed since the last time you asked the question, Senator. We will not be putting out guidelines until we know a bit more about what the actual section means. Similarly, we do not have guidelines out on the whole of section 46, for the same reason. So we are no closer to issuing guidelines than we were the last time you asked.

Senator JOYCE—But, Mr Cassidy, when will you be close to issuing guidelines? What are you waiting for?

Mr Samuel—The difficulty is that we have three tests there that are going to have to be subject to Federal Court determination to give us some guidelines in the first instance. It is no use putting out a guideline that says, ‘We believe relevant cost is as follows,’ when in fact I could probably provide you with three or four economic opinions that would give you entirely different views. It is no use saying, ‘We believe that “a sustained period” means as follows,’ when in fact a federal court may well determine in the circumstances that ‘a sustained period’ means something entirely the opposite. It is no use talking about what might be a substantial market share. We have indicated, for example—I have indicated in a number of public speeches—what might be a substantial market share, but I can tell you that there are as many different views about that within the organisation and within the legal profession as you might be able to count on your two hands and your two feet. These are matters that will ultimately be required to be determined by the court. If we were to put out a guideline that said—

Senator JOYCE—That’s very good.

Mr Samuel—Sorry, Senator—let me just finish. If we were to put out a guideline that said, ‘We believe that those three tests amount to the following,’ and then a matter were to come before us and we decided, ‘Based on a legal opinion it is appropriate to take it to court,’ and if then the court were to say, ‘ACCC, you were wrong; our view in the court is that a substantial market share selling below relevant costs for a sustained period means the following new guideline is wrong; you have given the wrong advice and we are going to hold the company concerned, the respondent concerned, liable and they face potentially a very significant penalty,’ that would not be a very comfortable position to be in. So I just do not think we can put out those guidelines, in all fairness.

Senator JOYCE—I am not going to engage with you on that because I concur with your view. That is surprising! But what I do say is: to remove ourselves from this conjecture, why don’t we take the case to court and sort it out?

Mr Samuel—Because before we can take a case to court we have to produce the evidence, submit it to legal counsel, and have legal counsel say to us, ‘Based on the evidence that you have provided, I consider that you have got reasonable grounds for instituting proceedings.’ That is a legal services direction that was issued certainly by the previous government and is maintained by the current government. And it is to stop vexatious or frivolous litigation by agencies which can be costly, both to the Commonwealth in terms of legal costs and to parties that might be the subject of our proceedings. So I think it is fair to say that we have not received legal advice of having reasonable grounds to institute proceedings in respect of any matter that has been the subject of investigation under Birdsville. I think that is correct—isn’t it, Mr Bezzi?

Mr Bezzi—I just wanted to add that, as the public servant in charge of the division that has to investigate these things, I am very keen to see the first case come up. We are progressing these matters at a higher than usual rate when you compare them to other part IV matters. I think I said 18 per cent of predatory pricing contacts are being progressed. But we cannot make these cases—they do not just come out of thin air. We have to find them, investigate them, and go through the proper processes and get advice that supports bringing the case.

Senator JOYCE—I understand that. In my paucity of experience in accountancy—and having solicitors in my office—if I ever got to a point of conjecture where I was trying to work something out, I would have to go through the trials and tribulations of paying for a legal opinion, from people who were more provident in their knowledge that I was, as to what the likely outcome would be. Have you tried to obtain that from external sources so that you can premise how you think the court would interpret the Birdsville amendment?

Mr Samuel—We do not just seek legal opinion from our solicitors; they will, in appropriate cases, seek legal opinion from senior counsel. But it would be a brave—in fact probably an improper—agency that would turn around and say, to legal counsel—senior legal counsel: SCs; QCs—‘We do not agree with you and we think we have got reasonable grounds for instituting proceedings and we intend to do so.’ In fact I am not even sure we can do it, can we?

Mr Cassidy—No.

Mr Samuel—We cannot do it.

Senator XENOPHON—Chair, can I ask a supplementary question directly on that.

CHAIR—Sure.

Senator XENOPHON—On how many occasions has the advice of senior counsel been sought in Birdsville type cases?

Mr Cassidy—I suspect we have probably got them in twice. I was going to say that we might have to take that on notice.

Senator XENOPHON—You believe it is twice?

Mr Bezzi—It has been at least once but it might be twice.

Senator XENOPHON—Okay—but it is in that order?

Mr Bezzi—Yes.

Senator XENOPHON—Thank you. Sorry, Senator Joyce.

Senator JOYCE—At least once and possibly twice—that is a lot.

Mr Samuel—You can take various statistics, and I think one of the compelling statistics is that the percentage of Birdsville type matters that are moved towards a more intensive investigation is, I think—correct me if I am wrong—about double the rate that occurs in relation to normal—

Mr Bezzi—Yes; 18 per cent instead of 11 per cent.

Mr Samuel—So it is getting close to double the rate that we would do. Some might even say, ‘Why are you increasing the percentage of matters referred to more intensive investigation under Birdsville, relative to what you do in respect of other anticompetitive conduct?’ You might smile and say, ‘Well, it is because Senator Barnaby Joyce is asking us to do it!’

Senator JOYCE—And other people. Nothing came to me via an epiphany. It was really by pressure from external parties—from Senator Xenophon and from small business groups, basically; that is how it came about.

Mr Samuel—But we are required, we are mandated, to pursue these matters with appropriate rigour, and the rigour means investigating thoroughly but, at the same time, seeking and obtaining the advice of senior counsel. And if senior counsel says, ‘You do not have reasonable grounds for instituting proceedings; you have not got a basis on whatever interpretation can be applied to those three tests—plus I have to emphasise the purpose test that is contained in section 46(1AA)’ then we are simply not permitted to commence proceedings. That is the simple fact of the matter. But if you take that statistic—18 per cent versus 11 per cent of initial investigations that are moved to intensive investigations in respect of Birdsville matters—then I think it is fair to say that it is getting well and truly the focus that it deserves.

Senator JOYCE—I tell you what: I am a betting person, and I can give you another bet. As long as I am here, I am going to pursue it.

Mr Samuel—That is one bet, Senator, that I won’t take with you!

Mr Cassidy—It’d be like betting on a one-horse race!

Senator JOYCE—In the recent dairy inquiry report by this committee, there were calls for Australia to have specific laws against anticompetitive price discrimination. Does the commission consider that anticompetitive price discrimination is outlawed by section 46 of the TPA?

Mr Samuel—I think it is inappropriate for us to comment upon the dairy report. We made some submissions to that committee, but really it is a matter of policy for government. There is—if I might say so, with the greatest respect—a degree of confusion in some of the recommendations of that report relating to issues of price discrimination and the like and what it actually means. You will be aware that the Australian parliament decided to remove the section 49 provisions relating to price discrimination back in the mid-1990s, following on from the Hilmer report on national competition policy, and I do not think there has been any suggestion since then that section 49 ought to be reintroduced. A long debate has occurred about that in many jurisdictions throughout the world. But I think it is fair to say that the general view on anti price discrimination provisions is that they tend to raise prices and operate in an anticompetitive manner rather than to lower prices and operate in a competitive fashion.

Senator JOYCE—But you would acknowledge that the evidence to the inquiry showed that the dairy farmers were being touched?

Mr Samuel—That is a separate issue. But you raise the issue of price discrimination: if we wanted to get into a debate about that, it would be interesting just to hear what your definition of ‘price discrimination’ is, and I suspect it may be of a different context or a different concept to that that some others might have. So I think we could get into a long debate about that. But that was the subject of a separate inquiry.

Senator JOYCE—Just going back to Birdsville: what educational activities have taken place to inform the people about Birdsville?

Mr Samuel—I and other members of the commission have given several speeches on that. Mr Bezzi, Commissioner Court and others have given speeches on the subject. We have endeavoured to bring a bit of rationality into the debate. It was initially subject to some irrational debate, not only I might say by some who were advocating the Birdsville amendment but also by some of those in big business who were opposing it. Some big businesses were suggesting that it had an excess of application. I think they have realised it is not true. There were others in small business who suggested it had a greater application than we thought on any reasonable analysis it could have had. Leaving aside our own analysis, there are several legal texts out there and legal opinions that have been expressed in various articles, journals and the like giving some views about what Birdsville means. I think you will find there is only one consistent view expressed in all of those journal articles and elsewhere—that is, no-one is very certain as to what it means at this stage.

That was inevitably going to be the case, Senator. You and I discussed this both privately and in a public sense at the time Birdsville was passed. We said it introduced some concepts into the law that were new and that were foreign. We said it would take some time for matters to get to the court for them to be established so that some jurisprudence could be established in this area. We knew that at the time.

Senator JOYCE—I concur with that. I am not going to argue with you on that point. ‘Some time’ is how long?

Mr Samuel—It is until such stage as: firstly, we can have a matter before us that falls within Birdsville—that is, the four heads that I have described, including particularly the purpose head that is often forgotten—secondly, the investigation is completed; and, thirdly, the matter is referred to legal counsel and we obtain advice that we have reasonable grounds to institute proceedings. We have gone through those processes, as Mr Bezzi has said, in respect of 18 per cent of matters that are the subject of initial investigation. But at this point in time we have not been able to produce a case where legal counsel has said, ‘You have reasonable grounds for instituting proceedings.’ I am sorry; I am repeating myself, which I am trying not to do.

Senator JOYCE—No, no. I and Australia can have confidence that you are taking it seriously, can’t we?

Mr Samuel—I would be amazed if you thought otherwise, Senator, after your repeated questioning on this subject in various Senate estimates hearings. If I might refer you back to the questions that Senator Brandis put to us at the last Senate estimates, which I thought made absolutely clear what our position was relating to the submission of matters to legal counsel. If I recall correctly, Senator Brandis asked the very direct question—and I asked him to clarify it—‘Have you received any advice in respect of any matter where counsel has said that you have reasonable grounds for instituting proceedings where the enforcement committee or the commission has determined not to institute proceedings?’ My clear answer to that was, ‘No, we have not.’

Senator JOYCE—That was a very precise question, wasn’t it?

Mr Samuel—It was a very precise question, and it was a very precise answer.

Senator JOYCE—It was exceptionally precise, if I might say so.

Mr Samuel—The question came from Senator Brandis, and the answer from me was very short and precise: no.

Senator JOYCE—Does section 46 cover anticompetitive behaviour?

Mr Samuel—Yes. It falls within part IV of the Trade Practices Act, which relates to anticompetitive behaviour. It covers a whole range of anticompetitive behaviour. In fact, in my opening statement I referred to the increased penalties that have been in place since 1 January 2007 and specifically referred to the misuse of market power provisions of section 46. It is an area where, as you would be well aware—because you have been sitting around this committee for some years now, as have I—we have had some degree of difficulty in tackling section 46 matters because of some interpretations of that provision by both the federal and the high courts but, as a result of amendments that were introduced by the former government and then further amendments introduced by the current government, we believe we now have a greater scope for instituting proceedings or for taking up matters under section 46 in respect of misuse of market power. It is a serious provision. It is probably second only to cartels—and I may be contradicted on this by my colleagues—in terms of its egregious form of anticompetitive conduct.

Senator JOYCE—Has the commission undertaken any investigation into allegations of anticompetitive price discrimination?

Mr Samuel—Again, I would perhaps be interested to get your interpretation of what—

Senator JOYCE—anticompetitive price discrimination is?

Mr Cassidy—That comes under section 46, Senator. I do not know whether my colleagues have it, but I do not know whether I have the information to say what period. It was an open-ended question.

Senator JOYCE—Let us take—

Mr Cassidy—Section 46 has been there since 1974.

Senator JOYCE—Thank you very much. I will not go back that far. I won't even do that to you, Mr Cassidy! Let us take the last 12 months.

Mr Cassidy—I will have to take that on notice.

Senator JOYCE—What about the last three months?

Mr Cassidy—We would still have to take that on notice to see if we had the information.

Senator JOYCE—Do you have any one before you at the moment? Do you have any case before you at the moment?

Mr Cassidy—At the moment we have 15 detailed investigations relating to section 46. Off the top of my head, I am not quite sure whether or not any of those 15 involve price discrimination. Let us take it on notice and we will give you an answer.

Senator JOYCE—Do you accept that the US and the United Kingdom have laws against anticompetitive price discrimination?

Mr Cassidy—Sorry? I can't—

Senator JOYCE—Do you accept that the UK, the United Kingdom, and the United States of America have laws against anticompetitive price discrimination?

Mr Cassidy—On specific laws, I must say that for the UK I am not sure. The US has the Robinson-Patman Act. I must say with the Robinson-Patman Act there have been a number of reviews over the years, including the recent congressional review of US antitrust law, which have all recommended that that act be repealed. Nonetheless, it is still on the statute books. So, yes, they do. As I say, for the UK I am not sure. But conceding that one for the moment I think we have toured a few countries that do have specific laws.

Senator JOYCE—Why haven't they repealed it?

Mr Cassidy—Sorry?

Senator JOYCE—Why haven't they repealed it? For all the jurisprudence—

Mr Cassidy—Again, in the US I think the reason why it has not been repealed has a lot to do with the processes in congress and the checks and balances that operate—

Senator JOYCE—What? Is public opinion against it?

Mr Cassidy—Sorry?

Senator JOYCE—Is public opinion against it?

Mr Cassidy—I would not say that. In fact, even the US Supreme Court has recently indicated—

Senator JOYCE—I was talking about public opinion.

Mr Cassidy—Sorry—I do not know. Could we answer a question? Thank you, Senator. The US Supreme Court has indicated that it will take a very narrow interpretation of Robinson-Patman and only in a sense find under it where it is quite clear that it has anticompetitive impacts.

Senator JOYCE—Does section 46 outlaw price discrimination?

Mr Cassidy—Yes, it does. It is covered by section 46.

Senator JOYCE—It does?

Mr Cassidy—It does.

Senator JOYCE—Has the ACCC received any complaints alleging anticompetitive price discrimination?

Mr Cassidy—I dare say we have. I cannot tell you the number. Again, I will take that on notice and give you a number if you like.

Senator JOYCE—Can the commission indicate the circumstances under which it considers that price discrimination can be anticompetitive?

Mr Cassidy—Where it results in a substantial lessening of competition.

Senator JOYCE—What does that mean?

Mr Cassidy—That is the test under the act.

Senator JOYCE—Tell me about it.

Mr Cassidy—Under the act, anticompetitive conduct is unlawful either per se, so called, which means it is outright unlawful—for example, price fixing—or if it results in, in the wording of the act, ‘a substantial lessening of competition’.

Senator JOYCE—Explain to me the term ‘substantial lessening of competition’. What does that mean?

Mr Cassidy—The way section 46 works is this. Section 46 is structured in terms of a ‘substantial lessening of competition resulting from predatory behaviour which has the effect of either eliminating a competitor, preventing a competitor from entering the market or preventing a competitor from competing.’ In terms of section 46, which includes, as I say, price discrimination, that is what ‘substantial lessening of competition’ means. It is one of those three things.

Senator JOYCE—Okay. Let us go through this ritual pas de deux. What is the threshold test?

Mr Cassidy—The threshold test is the one I just gave you. It is predatory and results in one of those three outcomes.

Senator JOYCE—What do I have to prove? I am Mrs Smith and I sell carrots at the store. What do I have to prove?

Mr Cassidy—Sorry?

Senator JOYCE—I am Mrs Smith. I work in the mall, the shopping mall—or whatever you want to call it. I know I am being shafted. What do I have to prove? What is my threshold test?

Mr Cassidy—What needs to be established is that the firm allegedly undertaking the price discrimination has significant market power and that the price discrimination was undertaken for the purpose of either eliminating a competitor, preventing a competitor from entering the market or damaging a competitor.

Senator JOYCE—Mr Cassidy, you are a smart man.

Mr Cassidy—Thank you, Senator.

Senator Sherry—How come I never get that?

Senator JOYCE—You just told me section 46 was a substantial lessening of competition test under section 46. That is correct, isn't it?

Mr Cassidy—No. What I—

Senator JOYCE—Hang on.

Mr Cassidy—Sorry, Senator. What I said was that the general test in the act—

Senator JOYCE—The general test in the act—

Mr Cassidy—is a substantial lessening of competition.

Senator JOYCE—The general test in the act?

Mr Cassidy—I started at the broad. I said you had two types of things. You had conduct, which is per se just straight out unlawful, and you had conduct which is unlawful if it results in a substantial lessening of competition.

Senator JOYCE—Tell me—

Mr Cassidy—Sorry, Senator. In relation to section 46, the way in which that substantial lessening test is embodied, if you like, is in those three predatory elements that I mentioned. You have to have one of those three to be in breach of section 46.

Senator JOYCE—So you are saying the substantial lessening of competition test is in section 46?

Mr Cassidy—No.

Senator JOYCE—It is not?

Mr Cassidy—No, it is not.

Senator JOYCE—It was there three minutes ago and it is gone already.

CHAIR—Senator Joyce, perhaps if you listen, it might help.

Mr Cassidy—I think this is the fourth time I will say this, but I suppose I will say it for the fourth time. The way in which that general test—

Senator Sherry—That is not a record that you are going to set.

Mr Cassidy—No. It will probably be asked a couple more times yet. The way in which that test is embodied in section 46 is in one of those three elements that I mentioned. Either you substantially damage a competitor, you prevent a competitor from entering the market or you prevent a competitor from competing.

Senator JOYCE—I am going to help you out here because there is no mention of a substantial lessening of competition in section 46 of the Trade Practices Act 1974, is there?

Mr Cassidy—No. There are those three elements I just mentioned.

Senator JOYCE—No, there is not. There is no mention of them. In fact, I will quote it to you. Do you want me to do that?

Mr Cassidy—Well, you can read out those three elements and maybe you will stop asking me about them. They are in section 46.

Senator JOYCE—So the misuse of market power is:

- (1) A corporation that has a substantial degree of power in a market shall not take advantage of that power in that or any other market for the purpose of:
 - (a) eliminating or substantially damaging a competitor of the corporation or of a body corporate that is related to the corporation in that or any other market;
 - (b) preventing the entry of a person into that or any other market; or
 - (c) deterring or preventing a person from engaging in competitive conduct in that or any other market.

There is no mention of the substantial lessening of competition test in section 46. Isn't that right, Mr Cassidy?

Mr Cassidy—Yes. I did not say there was, Senator.

Senator JOYCE—Yes, you did.

Mr Cassidy—No, I did not. I said—

CHAIR—Senator Joyce. Say it again, Mr Cassidy.

Mr Cassidy—Again, okay. What I said was the general test in terms of the act is a substantial lessening of competition type test.

Senator JOYCE—Type test.

Mr Cassidy—The way in which that is embodied in section 46 is through the three elements of either damaging a competitor, preventing a competitor from entering the market or preventing a competitor from competing. They are the three elements you have just read out to me.

Senator JOYCE—I am not going to pursue it. You are wrong. I am bigger than that. Can the commission indicate how many small business collective bargaining applications under the Trade Practices Act it has received since the last estimates?

Mr Cassidy—I note that the total of collective bargaining notifications has been 22 since the amendment was introduced. I am just not quite sure what it is since the last estimates.

Mr Chadwick—I probably do not have them with me here since the last estimates only.

Senator JOYCE—What does that mean? Just translate that. What does that mean?

Mr Chadwick—I think it means I do not have the figures here—we can take it on notice—of how many collective bargaining notifications there have been.

Senator JOYCE—You can take it on notice and get back to me.

Mr Cassidy—There have been 22 since the amendment was introduced. I do not think we know immediately how many it was since the last estimates.

Senator JOYCE—Can the commission indicate how many complaints it has received in relation to the Horticulture Code of Conduct since the last estimates, so we do not go back to 1974?

CHAIR—November?

Senator JOYCE—Since the last estimates.

CHAIR—February.

Senator JOYCE—I do not care—whichever one makes it convenient. Just give me a number.

Mr Samuel—Well, it had better be an accurate number.

Senator JOYCE—We are going all right so far. We just had a substantial lessening of competition test in section 46, so that was a big advancement. I will put that in the act tomorrow.

Mr Cassidy—Again, I do not think we have a figure since the last estimates. So we had better take that on notice.

Senator JOYCE—You had better take that on notice as well.

Mr Cassidy—In future, we will come along with a whole lot of figures about things that have happened since last estimates.

Senator JOYCE—While you are at it, how about the franchising code? How many of them since the last estimates?

Mr Gregson—We do have some figures of complaint data in relation to the franchising code.

Senator JOYCE—How many?

Mr Ridgway—From 1 January to 30 April 2010, we received 340 franchising complaints and inquiries, from which 10 initial in-depth investigations were commenced.

Senator JOYCE—There were 10 out of 340. I have found something now.

Senator XENOPHON—Mr Samuel, I have so many questions and so little time. I will start off with Golden Circle. Thank you for alluding to that. As I understand it, the company Golden Circle misled consumers because its cans said ‘proudly Australian owned’ when in fact it was taken over by Heinz back in 2008.

Mr Samuel—Correct.

Senator XENOPHON—As part of the penalty agreement with the ACCC, as I understand it, it was agreed that the company would donate about \$1.8 million worth of fruit and vegetables to charities.

Mr Cassidy—That is correct.

Senator XENOPHON—That is a fair summary. That \$1.8 million worth of produce that was given to charities probably would have been good PR for Golden Circle in itself. Did those cans have a label either crossing out or saying ‘no longer Australian owned’ so that consumers were not under misapprehension about that produce? The minister is smiling. It is an innocent question.

Senator Sherry—You are tough, I have to say.

Mr Cassidy—Are you suggesting, Senator, that the charities would have given it back had it been not owned here?

Senator XENOPHON—No, I am not suggesting that at all. All I am saying is that the whole idea of penalising—

Mr Samuel—No. We did not require that. This is an issue that was raised with me by a couple of sections of the media at the time we announced this. They said, ‘Well, you’ve given them a chance to get some good publicity.’ I have to say to you that I doubt that Golden Circle actually relished the publicity they got over this matter. It was widely publicised that they had been engaged in misleading and deceptive conduct. As I read it—forgive me, but one can only read the take that you get from the media—I think people generally took the view that this was a pretty good outcome. We got the \$1.8 million worth of cans given to charity and Golden Circle got some pretty bad publicity out of their misleading and deceptive conduct.

Senator XENOPHON—Just on this—and I have a couple more questions along this line—it is misleading because when the consumer goes into a supermarket they see a can that says ‘Golden Circle, proudly Australian owned’ when it was not the case. Consumers or those who have sought the help of a charity got a can as part of the penalty, and it is a Golden Circle can without a little sticker that would have said it is part of a penalty because it is not Australian owned any more. It could have been stuck on these cans. The whole idea of it was to penalise Golden Circle for misleading consumers. But then by distributing their cans as part of the penalty without any corrective labelling, was that unhelpful, do you think, in the context of consumers being continually misled as a result of that? There is a bit of irony.

Mr Samuel—No. I understand what you are saying.

Senator XENOPHON—There is some irony. It is somewhat ironical, though, is it not?

Mr Samuel—I understand what you are saying. But keep in mind this: had the matter gone to litigation, it would not, I think, on any reasonable basis have been possible to obtain an order that the \$1.8 million worth of cans of produce be distributed to charity or the like.

Senator XENOPHON—Please let me make it clear that I am not criticising the ACCC for the quantum in terms of the value of those cans. Was any consideration given by the ACCC to have some corrective labelling on the cans, which would have cost something but presumably nowhere near \$1.8 million?

Mr Bezzi—There was a requirement that corrective advertisements be put in newspapers. That was considered, I think, the most appropriate way of informing anyone who might get these cans that Heinz had engaged in misleading and deceptive conduct.

Senator XENOPHON—No consideration was given to putting a label on the cans?

Mr Bezzi—No. I do not think we thought of that. We were very keen to make sure that the impression was corrected. That is why we insisted on corrective advertising.

Senator XENOPHON—I am all labelled out. I just want to keep going on the issue of Leslie White's report that was in the *Weekly Times* of 27 May to the effect that the incorrectly labelled Golden Circle products are still for sale. You alluded to in your opening—

Mr Samuel—Yes. I mentioned that we are aware of that. We have communicated with Heinz and indicated that they need to complete the program of removal from the shelves. This is a bit of a stock rotation exercise, I think. Mr Gregson, did you want to comment on that?

Mr Gregson—We have been keeping an eye on the marketplace with a series of surveys across various stores. We have seen a decrease in the prevalence of the use of the representation. That is obviously a stock rotation issue. We are keeping a very close eye on that. As recently as earlier this week we have written to Heinz indicating that we are still finding small numbers of product on the shelves. Certainly we make no apology for their inability to get those off the shelf as yet. Obviously we will keep an eye on that closely. We put them on notice of our increasing concern.

Senator XENOPHON—So are they in breach of the undertakings or the agreement?

Mr Gregson—No. The undertakings require that they cease producing and providing or supplying these products into the supply chain. What we are talking about here is products that have been in the supply chain with retailers. There is a rotational issue.

Mr Cassidy—Stocking shelves is in the control of the retailers.

Senator XENOPHON—I understand that.

Mr Cassidy—But we have placed an obligation on them.

Senator XENOPHON—Given what Mr Bezzi said, is it unreasonable to require some further corrective advertising by the ACCC so that that is—

Mr Gregson—Indeed, the undertaking required a second set of advertising where there were still representations being made. Not only has there been a second set of advertising; we required a third advertising series as well, which went out not that long ago.

Mr Bezzi—And, I think, in-store corrective signage.

Mr Gregson—Certainly, if we identify an ongoing issue over the next few months, we will have to look at how we deal with that and what action we may or may not take.

Senator XENOPHON—Thank you. I want to go to the issue of whether the ACCC has received any complaints about misleading conduct in relation to online or other gambling services. I have had complaints from constituents over the years about services that look like a stock market service but in fact are about how to bet on the horses and indicate that it is a sure thing when in fact it is not. People do their dough. Is that in the statement?

Mr Samuel—You will find in my opening statement—a full copy of which has been given to you and will be put into *Hansard*—that we make reference there. For example, there is an action we took against a company or a website called ‘Powerballwin.com.au’, which was a scam. This was a website that claimed to predict numbers to help win all the divisions of Powerball in Tasmania. Within three days we actually obtained interlocutory injunctions to close that down. It was a website and servers. They were located in the UK and the USA to promote and run the scam. Justice Tracey of the Federal Court labelled the scheme as bogus, saying:

All too often, unscrupulous individuals seek to enrich themselves by devising schemes under which unsuspecting victims are induced to part with their money and other property.

So we are conscious of those and have taken action. What we tend to do in those is to do so in conjunction with our international counterparts, because very often they are run from outside Australia.

Senator XENOPHON—On a related issue, recently in the *Australian* Professor Kevin Harrigan from the University of Waterloo in Canada gave a number of lectures about the design of poker machines and features of near misses and losses disguised as wins, where you play 10 lines in a poker machine, you lose on nine but you win on one and it comes up as a win in terms of reinforcing that. Is this something that the ACCC has looked at? What liaison is there between the ACCC and various gambling regulators about issues of machine design? You may wish to take this on notice. It is a genuine question based on Professor Harrigan’s recent evidence in Australia about features and machines that could be inherently misleading to consumers.

Mr Cassidy—Yes. We will have to take that on notice.

Senator XENOPHON—Perhaps I will correspond with you further in relation to that. That would be useful. In answer to question No. 1 placed on notice in February, the ACCC stated that at the time it had spent \$313,924 of the \$1 million allocated to administer the unit pricing code of conduct in the 2009-10 financial year. Can you tell me how much more of that has been spent in this financial year? Can you give a breakdown of that money? Perhaps that latter part of the question could be taken on notice.

Mr Ridgway—We might have to take the question, which is back to the amounts expended, on notice.

Mr Cassidy—What we will have to do here is actually add up the different things we have done and what we have spent on the picture in total. It is not something that just falls out of our system.

Senator XENOPHON—Sure.

Mr Cassidy—Let us take it on notice.

Senator XENOPHON—Does the ACCC intend to hold a review of the code or undertake any monitoring to determine how useful the code is for consumers in the future?

Mr Ridgway—The ACCC has undertaken to do some survey work of compliance levels in the supermarkets that are subject to the unit pricing code.

Senator XENOPHON—I think that, in the answer to the questions on notice I submitted, the ACCC said it was undertaking a national survey of unit pricing. Has the survey been completed or is it close to being completed?

Mr Ridgway—The survey has commenced. It should be completed in the not-too-distant future.

Senator XENOPHON—Thank you. I want to move to the issue of petrol pricing. I understand that the ACCC provided—if I am wrong, I am sure you will correct me—a confidential report on anticompetitive behaviour in the petrol pricing market to the Minister for Competition Policy and Consumer Affairs in December 2009. Are there any plans to release this report publicly?

Mr Samuel—That is a matter for government.

Mr Cassidy—I would have to say that, if it were to be released, it would have to be somewhat redacted because it contains information that we had obtained under our section 155 powers. There is a specific legal prohibition in that section against making that information available other than to—

Senator XENOPHON—Perhaps I should direct it to the minister.

Mr Cassidy—But it is an issue for government.

Senator XENOPHON—In relation to the confidential report on anticompetitive behaviour in the petrol pricing market that was provided to the Minister for Competition Policy and Consumer Affairs in December 2009, is the government proposing to release that report, even in a redacted form, given that Mr Cassidy has said some aspects of it cannot be released?

Senator Sherry—I will have to take that on notice. I will personally discuss it with Minister Emerson and see how we can facilitate it.

Senator XENOPHON—Sure. I think many would say it is in the public interest for that report or even a redacted version to be released. I want to go back to the issue of unit pricing. How many complaints has the commission received in relation to possible breaches of the unit pricing code of conduct since the last estimates hearings—in other words, in the last four months?

Mr Ridgway—We have figures for the number of complaints we have received since 1 December through to May this year. We have a total of 33 complaints.

Senator XENOPHON—In that period. The commission would be aware of media reports on the weekend regarding errors by a major supermarket chain in the unit pricing of its online groceries. Is the commission investigating any possible breaches of the code arising from those weekend reports?

Mr Cassidy—Getting back to what the chairman said earlier, we would prefer not to comment on specific investigations. Let me give you a more general answer saying that we are actively monitoring unit pricing and its implementation. We have now just completed our third survey across all retailers looking at their unit pricing practices. The results of that are now being analysed, plus the results for the second survey, which we thought were pretty good in terms of the compliance levels. So, without commenting on the possibility of a

specific investigation, let me say that we are actively monitoring compliance with unit pricing. The way we do this with a new law is that we start with a heavy focus on education and compliance. But then, of course, as the law is established and settles in, we move increasingly from education and compliance to enforcement activities. Without wanting to, in a sense, prejudge what might happen in the not-too-distant future, let me say that I think we are starting to enter that transition period, given that the law has now been out there for a while.

Senator XENOPHON—I want to go to the issue of petrol. Can the commission indicate how much it has spent on the issue of petrol price monitoring and the monitoring of issues of competitive behaviour in the market, including the wholesale market, in the last 12 months.

Mr Cassidy—Again, can we take that on notice?

Senator XENOPHON—Sure.

Mr Cassidy—I just do not know that we have that level of detail with us.

Senator XENOPHON—In relation to the issue of price monitoring generally, has there been any analysis undertaken as to the efficacy of that? The ACCC undertakes price monitoring. Has the ACCC undertaken any study or surveys as to how effective price monitoring is? In other words, in terms of the behaviour of participants or the mere fact that you monitor prices, how effective is that in modifying or mollifying behaviour in the marketplace?

Mr Samuel—It depends on the area, Senator. I think that the general view would be that while price monitoring is regarded by some bodies and economic advisers as being relatively light-handed regulation, it can in many respects be a somewhat heavy-handed regulation because the obligations imposed on those that are the subject to the monitoring can be quite extensive and yet the impact of the regulation can, in fact, be quite minimal. You would be aware, of course, that we have conducted in the past various areas of price monitoring related, for example, to the insurance industry—to medical indemnity insurance and the like—although a lot of that has since ceased. The major areas of price monitoring we are engaged in at the present time relate to the stevedores, where we issue an annual price monitoring report. There are airports, where we do both price and quality-of-service monitoring, as well as airport car parks. In those areas, I will leave it for others to judge how effective they are. Each year we issue a report that indicates the sort of return on assets employed and the like, but I am not sure that the actual impact of the price monitoring report itself could be regarded as very significant, indeed, other than to expose the prices and pricing behaviour.

Senator XENOPHON—So that is its greatest value, in a sense?

Mr Samuel—Well, that is it; it is exposure. But whether the parties take any notice of it or not is another issue. There is one area where I think we have and can be effective, and that is in relation to our formal price surveillance, or price monitoring powers that might occur, for example, in relation to Australia Post. I think the activity that we have been engaged in there for the past six months has resulted in a significant level of improvement in the information that has been provided to the commission over issues of cost reductions, revenue declines flowing from the reserve services or the decline in the use of reserve services and potentially

even some revised management processes within Australia Post to deal with some cost restructuring.

Senator XENOPHON—Thank you. I have two or three more topics in the remaining time. You mentioned earlier the issue of mobile phone contracts. I think a bugbear of consumers is that they buy a phone, they sign to up a two-year service agreement, the phone goes kaput within 12 months and they are left high and dry. You may have seen the article by Sam McKeith in the *Financial Review* on Monday, 31 May, headed ‘Mobile safeguards will drop out’. It is asserted that consumers are set to lose protection against faulty mobile phones in terms of what is being proposed. Can you comment on that? Is it your understanding that what is being proposed will mean fewer safeguards, because many would be surprised at that?

Mr Samuel—Well, we were surprised as well when we read the article. The first thing I did was to say to colleagues in the office, ‘What have I not been informed about?’ because it was very surprising.

Senator XENOPHON—That is what I thought too.

Mr Samuel—I think it is fair to say that the article was, in our view, wrong. The conclusions drawn were wrong. It must be remembered, Senator, that what the article was saying was in a hypothetical set of circumstances: were the minister to exempt telcos from certain regulations under the Trade Practices Act, then under the new Australia consumer law there would be some gaps, if you like, in the enforcement. But I do not think it has ever been suggested that that might occur.

Senator XENOPHON—Thank you for that. If the minister did exempt telcos from certain requirements under the regulations, that could occur?

Mr Cassidy—The whole idea of exemption is that, say, a telco retailer cannot be held responsible for something which is not his fault. In other words, if a service is not provided because the carrier does not produce the carriage service, the retailer cannot be held responsible for that. That is what the minister has power to exempt. But it has nothing to do with faulty mobile phones, nothing to do with misleading ‘free and unlimited’ and so forth advertising. It is purely that sort of issue, where the retailer cannot be held responsible for something which is not his fault.

Mr Bezzi—The retailer of the service, not the actual physical phone.

Senator XENOPHON—Because of time constraints, if there is anything further the ACCC want to put, do. You were surprised and I was concerned when I read that. I am not saying that the journalist was inaccurate. I am just saying that it put a set of circumstances that—

Mr Samuel—I do not think it was the journalist so much as representations that had been put to the journalist by various groups, which we believe were wrong.

Senator XENOPHON—I think Mr McKeith fairly represented what was put to him—

Mr Samuel—Correct. We think that they were wrong.

Senator XENOPHON—to be fair to him. I want to go to the issue of geographic price discrimination. You are aware of the bill I have had with Senator Joyce in terms of the

Blacktown amendment. Is the commission aware of media reports also on the weekend regarding geographic price discrimination by liquor outlets owned by the same major supermarket chain? If so, is the commission concerned that consumers are paying a higher price for the same product in different locations?

Mr Samuel—I am aware of the article, Senator. I am aware that consumers do pay different prices in different locations for products and services. But, as I have said on a few occasions before and met the ire of some senators in so saying, there is no law that requires the same price to be charged across all geographic locations in Australia for the same product or the same service.

Senator XENOPHON—Has the ACCC welcomed the move by, I think, Coles and Woolworths to have uniform pricing over a number of their products throughout their stores?

Mr Samuel—In fact, we had this discussion, I think I recall, two Senate estimates committees ago, Senator. What I said—

Senator XENOPHON—It is an oldie but a goodie, though.

Mr Samuel—Yes. It is an old but good one. I think I indicated at the time that the general reaction from consumers seemed to be to welcome that. Insofar as consumers are better able to assess the competitive offerings of different suppliers and that is facilitated by having similar prices across geographic regions, so be it. But there is no process for the ACCC to approve or disapprove of geographic price differentials that are charged by suppliers. That is just not part of the act.

Senator XENOPHON—I understand that. But whilst you do not have a role in respect of that because there are no laws at the moment for uniform pricing, does the commission monitor claims by major supermarket chains insofar as they make claims that they have uniform pricing?

Mr Samuel—There is no question that if a claim is made that in marketing a product they have uniform pricing—

Senator XENOPHON—Which has been the case.

Mr Samuel—which is not the case—

Senator XENOPHON—But they have, have they not?

Mr Samuel—That is correct, yes. But if in fact it was demonstrated that that was not the case in practice, that may well form a basis for an investigation as to misleading and deceptive conduct.

Senator XENOPHON—That is right. My question is: given that it has been a marketing tool by a couple of the chains that they have the same prices across the metropolitan region across the state, has there been any monitoring by the ACCC of the veracity of those claims?

Mr Samuel—I think it is fair to say that since the claims were made so widely and so publicly, the matter has been under constant review by the commission.

Senator XENOPHON—Does ‘review’ mean—

Mr Samuel—A review means monitoring, watching and checking.

Mr Cassidy—We have checked, yes.

Senator XENOPHON—Perhaps on notice you could indicate the extent of checking in respect of that.

Mr Samuel—Yes, without going over the line of not commenting upon matters we may or may not be investigating.

Senator XENOPHON—Sure. I understand the constraints. I think the Chair might be generous in giving me one more minute. Can the commission indicate the number of complaints it has received on country-of-origin claims since the last estimates, in terms of food labelling?

Mr Samuel—We will have to take that one on notice, I think.

Senator XENOPHON—Dr Neal Blewett for COAG is looking at the issue of food labelling. Has the ACCC had any role in that, in terms of any proposed changes to laws and giving advice as to any new framework?

Mr Cassidy—On the second part, Senator, we have not made a formal submission to the Blewett inquiry, but we are scheduled to meet with the inquiry shortly to go through a number of issues that they want to raise with us.

Senator XENOPHON—I think my time is up. I have put a number of questions on notice. Thank you.

Senator PRATT—Thank you very much, Chair. I want to ask the ACCC how many people it is aware of who are currently falling victim to phishing, mishing and vishing scams. How are you going in managing that problem? Is there a particular profile of who is likely to fall victim and how they can be best assisted?

Mr Gregson—Senator, I might be able to assist you with that. In March this year, the ACCC put out a report in relation to its scam activity. That will have the full stats in relation to the number of consumers who complain to the ACCC together with the amount of losses reported by those consumers. The second part of your question was?

Senator PRATT—I am interested to know if there is a particular profile of consumers that are more likely to be vulnerable to that.

Mr Gregson—We make it a practice of advising that scams hit the wide cross-section of the community, from those who might be particularly well-informed or educated to those who may not, across all demographics. Of course, there are certain vulnerabilities that certain scams may prey on, but we are particularly keen to stress that everyone can be the victim of a scam. That is apparent in all our publications.

Senator PRATT—Yes. I have certainly seen that. Clearly education and trying to get a general awareness out there is part of that. What is the approach to this issue?

Mr Gregson—We take a number of approaches to any issue of compliance with the law. In relation to scams, we combine both our publications, presentations and various outreach activities, including our SCAMwatch work. We also participate in liaison activities with other regulators through the Australasian Consumer Fraud Taskforce and other networks. We also take matters through disruptive activities, be that bringing down websites or, alternatively,

dealing with either mail or other means of communication. Finally, we do take the pointy end of enforcement action.

Senator PRATT—Clearly there are a number of different technologies that are platforms for this activity today and there is a diversity to those platforms, be it mobile phones or laptops. There is a bunch of new devices coming into the market, be they iPhones or whatever. In a sense, the sellers of that technology have, in most instances, some control over some of the products and platforms that are available within their device. They can apply their own ethical standards to what is available there. Is the ACCC looking at working with the providers of this technology so that they are educating their own users as more and more of these different devices come online?

Mr Gregson—Enforcers around the world are more and more becoming aware that working with enablers or facilitators in the marketplace is a key issue for enforcement and compliance. We are looking at a range of bodies that we can be working with. I am not specifically aware whether we have approached manufacturers of devices or not. I should say we also attended the House of Representatives inquiry that dealt with some of these issues and provided information to that committee as well.

Senator PRATT—That is good to know. I do note that the ACCC is getting quite active now in different forms of social media, which is good to see, and that there are a number of other institutions and consumer agencies around the country doing the same thing. I am interested to know the ACCC's approach to being a body there to protect consumers. How does the ACCC see these social media platforms actually being able to draw more information from consumers and get them to more actively work with each other and inform each other, be it on things like sharing prices or any number of different things?

Mr Ridgway—The ACCC has recently made a conscious entry into what is characterised as the social media platforms, such as Twitter, for example, and some of the forums. We have started that with our product safety function because we feel it is increasingly an area where the consumers that we are trying to reach are informing and talking and sharing with each other. We track some of that communication. Recently, our launch of the review of our recalls function generated a very large volume of interest on Twitter and on social websites more generally. We will be looking at other opportunities to use that format. Interestingly, my observation is that some of the mainstream media coverage actually reinforced and encouraged the online forms to generate, so there is an interaction between the two.

Senator PRATT—Great. Thank you.

Senator COLBECK—I am anticipating that I might end up with a similar answer to the one that Senator Macdonald got earlier, but that is okay. Can I deduce from the answers you gave to Senator Xenophon and Senator Pratt that it is not necessarily a specific complaint that brings scrutiny from the ACCC into a particular matter? How do you actually engage with a particular circumstance that might be occurring? What would be the circumstances that would bring your attention to a particular matter?

Mr Samuel—There would be a range of what are called initiation processes that could apply. More often than not, it will come from the many, many tens of thousands of calls that we receive into our info centre, which then go through a process of consolidation and then

reference, as may be appropriate, to our investigators for either an initial or a more comprehensive investigation, as the matter proves up. But we also receive advice or complaints from competitors. We will receive advice, indeed, from members of parliament, who are receiving it from their constituents. We will receive advice from overseas counterparts—that is, our counterparts overseas. Members of the organisation, of which there now total in excess of 800, are constantly keeping their eyes open on a daily basis through their daily activities, whether it is walking through supermarkets, reading the newspapers, listening or watching radio or television advertisements for issues that flag concerns. Very often they will arise in that fashion.

Senator COLBECK—So there are a number of flags that actually raise particular issues to you. You have mentioned some that are of interest. Specifically with fairness of contracts and contract conditions, are there any parameters within which you would look at those particular matters? You have had some discussion about, say, franchising codes and things of that matter. But in other arrangements, do you actually look at fairness of conditions of contract as part of arrangements between parties, particularly a larger organisation that might impose conditions of contract on subordinates?

Mr Samuel—We will certainly be looking at those a lot more carefully as from 1 July this year, when the unfair contract legislation comes into place. But at the present time I think it is fair to say that with the exception of Victoria—

Mr Bezzi—Well, unless you are talking about unconscionability.

Senator COLBECK—So within those test parameters that you were discussing earlier?

Mr Cassidy—The unconscionability provisions are really about conduct—I am sorry to put it this way—which is beyond conscience, which is so harsh or oppressive that you could not say that it is in any way part of normal commercial dealings. There are provisions relating both to business transactions and unconscionable conduct in consumer transactions.

Senator COLBECK—So in a business transaction, what would be the sort of test that you would apply for that?

Mr Cassidy—Well, the act actually gives a number of issues to be considered in thinking about whether behaviour is unconscionable or not. I suppose the issue which makes it challenging is that the unconscionable conduct can be very specific to the individual facts of the case. So it is difficult to say in an across-the-board sort of way—

Senator COLBECK—So it is a particular judgment issue depending on the circumstances that you are provided with on a case?

Mr Cassidy—Yes. So it is difficult to say, ‘Look, this sort of conduct would always be unconscionable’ because it really depends on the facts of the particular case.

Senator COLBECK—Yes. I understand.

Mr Cassidy—But that is a relevant provision. We do not actually get into what you might call fairness issues because really they are more contractual sort of issues. It is really only if it goes beyond fairness, as it were, to something which is really grossly unfair, if I can draw that distinction.

Senator COLBECK—And that becomes a bit subjective and in a lot of circumstances a matter of judgment. People do not see it as being unfair, but within the scope of the act it is not necessarily deemed to be unfair.

Mr Cassidy—That is right. In fact, if you like, one of the issues we consider in relation to unconscionable conduct is not looking at the conduct in absolute terms. But is it, if you like, unfair or grossly unfair in the context of the industry in which it has occurred? Quite often, as you would appreciate, behaviours can vary from one industry to another depending on how competitive the industry is and a whole range of factors, really.

Senator COLBECK—So a practice that had occurred a number of times before but had not been challenged may actually get by because it is something that has happened before in the industry?

Mr Cassidy—Not necessarily. The fact that it has happened previously does not necessarily make it right. I will try to give an example. My colleagues are looking blank-faced at me, so I suspect they cannot really think of one.

Mr Samuel—Perhaps, to give you an example, in the fridge case—

Senator COLBECK—I have my copy of your notes open to that particular case.

Mr Samuel—I do use the words in the opening statement there, which I did not read out. But it is the overall factual matrix, which probably does not help you at all other than to say that it is looking at the totality.

Senator COLBECK—I understand. I get a sense of what you are saying from that perspective. What I am looking at is a circumstance—and I do not know whether they would be called a franchise or how they would be termed. I suppose that is one of the issues that will define how the case is particularly looked at. But the major company controls whether you have a business, the size of your business, what you sell your product for and, if you want to sell your business, who you can sell your business to and whether you have a business at the end of the day, even after a long period of time. A layperson like myself might make a judgment as to what is fair. I obviously do not think this circumstance is fair. I do not know whether it is actually a franchise arrangement and whether that makes a difference or not.

Mr Cassidy—I was going to say that it does in the sense that there is a franchising code of conduct.

Senator COLBECK—Yes. That is why I was asking that question.

Mr Cassidy—In a sense, the franchising code of conduct would not necessarily say that those things are prohibited. What it would say is that, look, the franchisee has to be told about these things before they enter into the franchise. They have to know what the deal is.

Senator COLBECK—Including, say, taking out a large chunk of the business with a period of notice, even though that notice might have been in the contract. Again, that comes back to the fairness of the contract issue that I asked about before. So a large chunk of their contract has been taken away, which effectively devalues the business to a certain level. Then they are told they may not have a business at the end of that current round. They have got to sell it to someone else, but it is at a reduced value.

Mr Samuel—Look, it might be appropriate, rather than trying to discuss the matter in very hypothetical terms, if you refer the matter to us. We could give you some advice on it.

Senator COLBECK—I assume I would get a similar answer to Senator Macdonald if I asked you whether you were dealing with National Foods and their vendor network around the country.

Mr Samuel—Yes. That is correct. You would get a similar answer to what we gave Senator Macdonald.

Senator COLBECK—Perhaps there is some notice given. If you are not, it is a rich minefield, in my view.

Senator BUSHBY—I thank the ACCC for assisting us today. I have one question from your opening statement. I notice you mentioned some successful cartel prosecutions that you have undertaken recently. One of them was Admiral airconditioning and others. You noted a major cartel prosecution against 17 companies and 22 individuals involved in collusive tendering for airconditioning contracts for schools, hospitals and shopping centres in Western Australia. That just sparked a thought in my mind. I was just wondering whether you had any cause, from public statements, publicly revealed facts or complaints that have been actually put to you, to look into or investigate anticompetitive behaviour in relation to the Building the Education Revolution buildings and the tendering processes that that involved, whether through managing contractors or subcontractors or others.

Mr Samuel—I think it is fair to say that the extensive publicity that has been associated with that has not gone unnoticed. We constantly have a vigilant lookout for any potential collusive operations that may occur there, but I do not think it is appropriate to make any more comment than just that.

Senator BUSHBY—But you are alert to the potential? Certainly the newspaper article suggests that there is activity going on which may—

Mr Cassidy—Is that the article in the *Weekend Australian* on 10 April?

Senator BUSHBY—I am not talking about any particular article. I think there is a number of articles that you can probably point to.

Mr Cassidy—There was a specific article which we did investigate. I must say we found that what was said in the article just did not have substance. We have had other complaints, and we have seen other press reports. We either have or we are investigating them.

Senator BUSHBY—On the face of it, what is being said publicly, I would think that a prima facie suggestion at least of potentially anticompetitive behaviour has been raised. It is certainly something I would have thought would be of interest to the ACCC.

Mr Samuel—Certainly the matter has not gone unnoticed.

Senator BUSHBY—Thank you. In your opening statement you also talked about the penalties that you have available to you. I wonder how much you raise from penalties and what happens to that. Does it go into consolidated revenue or do you keep it to use for enforcement purposes?

Mr Samuel—No. We do not operate like an investment bank on the basis of a success fee. Everything that we earn by way of penalties goes into consolidated revenue.

Senator BUSHBY—Which is what I would imagine would be the case. How much do you raise?

Mr Cassidy—It has been on the increase. I am sort of glad you asked this question, really. If you look at our funding, over the last six years to last financial year, our gross funding has increased by \$58 million, but as a result of our steadily increasing penalties, which go straight to consolidated revenue, the net increase over that period has only been \$21 million. Last financial year, we had something in the order of \$45 million in penalties. The year before that it was \$62 million. But with the new higher penalty regime that the chairman referred to kicking in, we would expect that it would be—

Senator BUSHBY—When does that kick in, or has it?

Mr Cassidy—Well, it is in now.

Senator BUSHBY—Have you had any successful prosecutions that have enabled you to take advantage of that yet?

Mr Cassidy—No. We have three cases in court at the moment which would all be subject to the new penalty regime, but none of those cases has yet reached judgment. I say kick in because as time goes on, more and more conduct will be subject to that higher penalty regime. We would expect that our penalties that we are returning to consolidated revenue will steadily increase.

Mr Samuel—Have you got an EBIT margin calculation there, Mr Cassidy?

Mr Cassidy—No. But I am sure I could come up with one.

Senator BUSHBY—I am sure the government appreciates the contribution. I understand the ACCC maintains a record of its use of its coercive powers. Is that correct?

Mr Cassidy—That is correct.

Senator BUSHBY—Which I think is a very good thing for transparency. When you have coercive powers at your disposal, I think it increases the degree of confidence of the public that they are being used properly if they can actually see where they are being used and when. I was just thinking also in the interests of transparency, you mentioned in your opening statement again that there was a lot of merger consideration that goes on that is not publicly reported for various reasons. Do you actually report that in any shape or form, even if you do not actually disclose the details?

Mr Cassidy—We, of course, have an annual report, but also we do—

Senator BUSHBY—In that annual report, do you actually quote the numbers of matters that you dealt with?

Mr Cassidy—Yes, and indicate time periods. I am not quite sure how widely it is appreciated, but we also do like a quarterly annual report.

Senator BUSHBY—The reason I ask that is that Mr Samuel made the point that a lot of these things happen that do not get reported. When you say they are not publicly noted, you are saying they are reported and it is not publicly noted?

Mr Samuel—No. I think what I said was that there are a lot of things that are reported that are not taken notice of in calculating some of the statistics.

Senator BUSHBY—That is fine. That explains it.

Mr Cassidy—I hate to be a nuisance, but have we got a quorum at the moment?

Senator ABETZ—Yes. We have a government senator present, and there is always a quorum until one is called.

Senator BUSHBY—I seek an update on the investigation into the practice of making new release DVDs available to consumers at sub-wholesale prices. This has been raised previously at estimates. Can the commission update the committee on the commission's investigation regarding supermarket chains offering DVDs at greatly reduced prices?

Mr Cassidy—We have now concluded that investigation. Basically three sorts of allegations were made. One was of predatory pricing, and it was made against Coles and Woolworths. One was of bait advertising. That was made against Coles and Big W. The third allegation was of misleading and deceptive conduct, and that was made against Coles and Woolworths. Briefly, in relation to predatory pricing—this relates a bit to the discussion we were having with Senator Joyce earlier—we were not able to establish the elements of predatory pricing in terms of, if you like, the Birdsville amendment for a sustained period. The special offer of \$5 CDs, if one can call it that, was made for only seven days. We did not think that would be a sustained period.

On pricing below relevant cost, our investigation revealed that it was not pricing below relevant cost. There was an issue of rebates. When you take the rebates into account, we were satisfied that they were not pricing below relevant cost. In terms of predatory behaviour, the offer was on the basis that you had to buy either \$80 worth of groceries from Coles or \$100 from Woolworths; it could be the other way around. It was open for only seven days and it was only on certain CDs. When you put those things together, we thought it was going to be fairly hard to make an issue that that was predatory behaviour, because that is not the way someone would behave if they were actually seeking to damage a competitor. So we satisfied ourselves that there was not evidence of predatory pricing.

Bait advertising is basically advertising something and then you do not have sufficient stocks. When someone walks in to buy it, they are told, 'Oh, well, we don't have that, but we have this other one which is the same'—which happens to be at a higher price.

Senator BUSHBY—To get you into the store.

Mr Cassidy—Yes. The offers were made with various caveats about 'while stocks last' and a 'limited number per customer'. Our investigation revealed to our satisfaction that there were reasonable stocks on hand of the CDs, although, of course, they did tend to go fairly quickly. So we were satisfied on that. In relation to misleading and deceptive conduct, that related to a claim made by both Coles and Woolworths of 'lowest price guaranteed' on the particular DVDs. I would probably prefer not to say too much about that because it is actually a case

before the courts. Aldi has taken its own proceedings against Coles in relation to that particular allegation. So I think in the interests of that case it would probably be better if I did not say too much about that other than the fact that we have concluded our investigation in relation to that particular allegation.

Senator BUSHBY—So I take it from what you said there that one of the key aspects was the fact that it was a short promotional type of thing rather than—

Mr Cassidy—Yes, it was short. It was still a high entry to get to it in terms of the groceries you had to buy.

Senator BUSHBY—If they started doing that regularly, would that warrant a further look?

Mr Cassidy—I think the short answer is yes. One of the issues—again, particularly with the Birdsville amendment and sustained period—is that part of the thinking we have had is that a sustained period may not just be a continuous period of time. If you had a series of periods occurring one after the other, that could start to take you into that sort of sustained period territory.

Senator BUSHBY—Can the commission indicate if the supermarket chains lodged a notification under the Trade Practices Act in relation to exclusive dealing involving the DVDs?

Mr Samuel—We are not aware that they have, Senator.

Senator BUSHBY—But you can check it and take it on notice, just to make sure? Thank you. Can you indicate the length of time it took to investigate the matter?

Mr Cassidy—Sorry?

Senator BUSHBY—The length of time it took to investigate.

Mr Bezzi—We received the matter on 9 December and we closed it on 24 March.

Senator BUSHBY—I have some questions about so-called telecommunications scams. Can you indicate how many complaints the commission has received from small businesses in relation to telco finance scams, where cheap calls are offered and so-called free plasma TVs or similar equipment are offered as part of the deal?

Mr Gregson—The ACCC has a matter before the courts involving allegations similar to that which you have raised. We have received a large number of complaints not only in relation to those matters before the court but also in relation to perhaps similar conduct.

Senator BUSHBY—Can you indicate the scale? What does ‘a large number’ mean?

Mr Gregson—I might have to take that on notice, Senator.

Senator BUSHBY—Are we talking tens, hundreds, thousands?

Mr Gregson—I think we will take it on notice, Senator—but certainly more than tens.

Senator BUSHBY—Obviously you have investigated those to some extent because you have a matter before the court. I presume that there are other cases or other allegations that have been raised that you are currently looking into as well?

Mr Gregson—Certainly; we look at a number of those complaints. We also look at other ways of ensuring compliance outcomes not only by education but also by working with others in the industry to try to address some of our concerns.

Senator BUSHBY—Is there anything that you can do or are doing to practically help those small businesses that have been subjected to these arrangements?

Mr Gregson—There are. In addition to our own proceedings, you may be familiar that private parties have considered proceedings and have approached the ACCC in relation to assistance we might be able to give in those proceedings. We have been talking to those small businesses. We have also provided extensive information about our concerns and the type of issues they should be looking at together with the compliance and educative work that we are doing around this issue. I should note, Senator, there has been a significant interest from a number of parliamentarians. We have been providing that information as requested.

Mr Samuel—I think it is perhaps also appropriate to indicate that we have had high-level communications with several of the finance companies that are involved or banks that are involved in these sorts of bundle processes. They indicate that they consider it seriously whether they pursue the completion or the fulfilment of finance contracts where there has been a failure on the part of the telco concerned to provide the relevant services. I think it is fair to say that those discussions could currently be described as being constructive but ongoing.

Senator BUSHBY—Progressing, yes. That is good news, I think, for the small businesses involved. I hope that works through well. Can you update the committee on progress with the ACCC's investigation into whether the North West Shelf joint marketing arrangement for gas into the WA domestic market should continue?

Mr Gregson—Mr Chadwick might add to this. The North West Shelf has applied for authorisation in relation to its arrangements, which very much, I guess, deals with the issues that we would have been looking at under any investigation.

Mr Chadwick—The North West Shelf did lodge an authorisation application on 31 March. We are currently undertaking our public consultation process in relation to that application. We currently expect to issue a draft decision in June or July.

Senator BUSHBY—You are answering my questions so well that you are answering my subsequent questions as well.

Mr Samuel—We have not yet learnt to anticipate your questions.

Senator BUSHBY—You do well with Senator Joyce. Is the ACCC considering the Senate's December 2008 report into the joint marketing arrangements on the North West Shelf project as part of its deliberations?

Mr Chadwick—Sorry, Senator; I did not quite catch that.

Senator BUSHBY—Is the ACCC considering the Senate's December 2008 report into the joint marketing arrangements on the North West Shelf project as part of its deliberations?

Mr Chadwick—We will have regard to the full range of views.

Senator BUSHBY—You were aware of that already?

Mr Chadwick—Yes.

Senator BUSHBY—I refer to media reports, such as the 31 May *Australian Financial Review* article titled ‘Pricing heat on North West Shelf gas partners’, where the argument seemed to centre around not renewing the approval for joint marketing arrangements to provide competition to drive better prices for consumers versus the added cost and risk of separate marketing pushing up prices to consumers. How is the commission weighing up these competing arguments—the claims of much higher prices in the west compared to the east coast and price hikes in the last 18 months?

Mr Chadwick—I guess it is a bit hard to comment on those sorts of issues because they are precisely the types of issues the commission is considering. When the commission makes its decision, it will put out a draft decision and then give interested parties an opportunity to comment on the commission’s preliminary views before formulating our final views. So people will have an opportunity to comment on the commission’s preliminary views when that draft goes out.

Senator BUSHBY—When you do make a decision, will you publish that and publish the reasons for the decision?

Mr Chadwick—That is exactly right, and, indeed, put out a media release so it is well known.

Mr Cassidy—It has turned out to be a transparent sort of process under the legislation, so submissions we receive, unless we deem they are generally confidential, will go up on our website. We have to put out a draft determination. We have to give interested parties the chance to be heard on that draft determination. Then we put out a final determination. So, if you like, it is there for everyone to see in terms of the process and in terms of the submissions. Actually in our draft determination we give a fairly full outline of the way we have considered the competing considerations.

Senator BUSHBY—Good, thank you. I will change the subject: what is the status of activity to remove restrictive covenants at shopping centres that have been identified as a barrier to competition to major supermarket chains?

Mr Samuel—Well, across-the-board agreement has been reached and undertakings have been given for the removal of the restrictive covenants in accordance with, I think, what I indicated at the last Senate estimates, which covers all the major supermarket chains. That is not just the very large ones but also some of the smaller supermarket chains throughout the country. You are aware of the 20 per cent—I think we talked about this last time—that are going through the gradual expiry process over the transition period; that is, the more recent covenants entered into. But it is fair to say that I think, with one exception, restrictive covenants across the board in respect of grocery outlets have been removed.

Senator BUSHBY—I understand that the ACCC is currently looking into the family that owns about six supermarkets in Canberra and Sydney. It is about the supermarket premises they took over from one of the big chains in the Canberra Centre that is next door to Aldi in the same complex and in close proximity to a number of major competitors. Is it the case that the ACCC is forcefully pursuing an undertaking from the independent supermarket owners about the restrictive covenant they inherited when they took over the vacated site?

Mr Samuel—I think the only comment I can make is that the only supermarket chain that has not provided a voluntary undertaking in respect of this matter at this point of time is the Supabarn group in Canberra.

Senator BUSHBY—Has the ACCC agreed to extend time available to the family to respond to the commission's demands for an undertaking?

Mr Samuel—I do not think I can make any further comment at this point of time, given that it is not our practice to comment upon matters that we may or may not be investigating.

Senator BUSHBY—Okay, I will leave the rest of those questions. In relation to small business related investigations, does the commission have any benchmarks in place for indicative timeframes for completing investigations?

Mr Gregson—The ACCC, and indeed in our enforcement areas, does endeavour to complete investigations in a timely manner. Of course, investigations dealing with different issues will take different times, so it is hard to be precise. But we certainly endeavour to complete those investigations in a timely manner. But that would be influenced by a number of factors.

Senator BUSHBY—Which can be as long as a piece of string. I am not suggesting that you deliberately do that.

Mr Samuel—No. I just want to add to that because it is important to understand the processes that have been put in place over the past four or five years. But we have, as you are aware, offices right throughout the country in every capital city as well as in Townsville. The investigations encompass a group of, I think, something close to 300 staff.

Mr Bezzi—Around about that.

Mr Samuel—Around about 300 staff in the country. What we have put in place over the past four or five years is a fairly effective process of central data control and management. If we consider that at any point of time there may well be 600 or 700 matters that could be the subject of investigation, then of the order of 150 to 200 matters could be under intensive investigation. I have likened it in past discussions before Senate estimates to a large legal firm that has a large number of files which does require some central control and management. That is done under the supervision of Mr Bezzi and Mr Gregson in particular and the enforcement committee. I think we have a very good handle on the time processes that are occurring and the time lines that are occurring with respect to investigations. The efficiency associated with that has improved very dramatically over the past four or five years since that central data control and management process has been put into place.

Senator BUSHBY—So that is an administrative control?

Mr Samuel—That is correct, yes.

Senator BUSHBY—Do you have resource constraints that actually limit your ability to move things through as quickly as you would like? Is it a matter of balancing priorities in terms of that or is it really just a matter of other extraneous factors that are in place and beyond your control that put time constraints on how quickly you can deal with these things?

Mr Samuel—Look, I am always hesitant, particularly on the public record, to say that we do have sufficient resources. You always like to convince the finance minister that we have insufficient resources. But I think it is fair to say that the investigations in many cases can be very complex. They can be hampered by resistance on the part of parties against whom allegations of misconduct might be being made and/or the difficulty of either locating witnesses or getting witnesses to agree to come forward. I think, as I indicated before, that particularly in the areas of unconscionable conduct and in a range of other areas parties that have been subjected to the sort of conduct that we might be investigating are often somewhat concerned about having to spend time and become involved in an investigative process that may well find them in court having to give evidence in circumstances they do not find comfortable. So there are a whole range of extraneous factors that can influence the process. But I do think it is fair to say that the mechanisms, the processes and the controls that have been put in place are designed for and have, I think, achieved quite well the outcome of timeliness that we have considered to be very important.

Senator BUSHBY—That is in a general administrative sense. Do you actually look at particular cases that may, because of the circumstances surrounding the allegations, need to be addressed urgently and actually give them a priority in terms of dealing with that?

Mr Samuel—I think it is fair to say that every single matter that is under investigation receives at least on a monthly or bimonthly basis the specific attention of our most senior managers, the enforcement jurisdiction, to undertake the timeliness of the investigative process. But at the same time, where there is a matter that requires urgent attention—that is, in a matter of days—we are now facilitated in taking interlocutory proceedings by some amendments that were made to section 155 of the Trade Practices Act. They enable us to commence interlocutory proceedings and obtain interlocutory injunctions, for example, to stop conduct that might be egregious and that the court considers ought to be restrained. We can take that course of action without substantially inhibiting our further investigation that might lead to the substantive court action. There are some limitations that are associated with those amendments, but it is fair to say that they have given us an opportunity to pursue those courses of action. I think I mentioned one or two of those in the opening statement.

Senator BUSHBY—I am conscious of time and that Senator Abetz and Senator Milne still have questions, so I will quickly run through mine. I could ask some more about that: can the commission indicate if it has identified any trends in relation to particular types of small business related complaints?

Mr Gregson—The nature of complaints that come from small businesses obviously raises issues on the day. There are certainly issues that come up at any particular time that are current. I am not sure we have picked up any other particular trends, but we certainly learn lessons from both the matters that come before us and the way we investigate them.

Senator BUSHBY—Can the commission indicate whether it advises small business complainants to pursue mediation as a precondition to the commission investigating a small business complaint?

Mr Samuel—Certainly not as a precondition, no. But in appropriate cases, it may well be that we would try to direct parties or advise parties to go into a mediation, particularly where

there would not appear on the surface to be a direct breach of the Trade Practices Act involved or the various codes of conduct. In some cases, we may even assist in bringing about that mediation process. But it is certainly not a precondition to investigation.

Mr Cassidy—Particularly in relation to the codes—the franchising code, the horticultural code and the petroleum industry code—because there are mediation processes provided for each of those codes.

Senator BUSHBY—Is it a precondition in those codes?

Mr Cassidy—No, it is not a precondition either. But, depending on the nature of the complaint, quite often they can be resolved more quickly and cheaply through that mediation process than, say, if the matter were to proceed to litigation.

Mr Bezzi—I will just add in relation to franchising that it is usually a continuing relationship, so the last thing that the parties really want is to be in protracted litigation. They really need to try to resolve the thing quickly through a mediator, if possible. So while we do not require it, often people are encouraged to facilitate it.

Senator BUSHBY—On those codes, has the commission received any formal complaints from mediators under any of them—the franchising, oil or horticultural codes—particularly regarding possible breaches?

Mr Cassidy—We refer obviously to a lot of mediators, where we have a complaint that we think is suitable for mediation. Similarly, the mediators, if they have someone come in where the conduct is basically fairly egregious, they will say to them, ‘Look, we think this is a matter that you should be taking up with the ACCC’, and they will cross-refer to us. So we do have those arrangements with each of the mediators.

Senator BUSHBY—What about regarding specifically possible breaches of the dispute resolution processes under those codes?

Mr Samuel—Well, if it is a breach of the code itself, it is more likely to be referred to us for enforcement action, being a breach of the code.

Senator BUSHBY—By whom? The mediator?

Mr Samuel—Generally what happens is that the mediator discerns that the dispute cannot be resolved and/or that there is a breach of the code that is involved. That may be referred to us for appropriate investigation and enforcement action.

Senator BUSHBY—Can the commission indicate how many complaints it has received in relation to possible breaches of the dispute resolution processes under those three codes?

Mr Samuel—I would have to take that on notice.

Senator BUSHBY—Has the commission ever conducted a full investigation into specific alleged breaches of the dispute resolution processes under the codes?

Mr Ridgway—In my experience, the number of concerns that we have had raised with us directly related to conduct in relation to the mediation requirements have been resolved upon contact from the ACCC to the other party to clarify their obligations on the one hand where it has been perhaps unclear to them. Increasingly, the trend has been under the franchising code for franchisors to raise concerns about franchisees not meeting the obligations they feel they

should be meeting. Sometimes clarification has assisted. On other occasions, it has become apparent that the concern has not been substantiated so it has not required further investigation.

Senator BUSHBY—Well, that is very useful. So the answer ultimately is that you have not actually conducted a full investigation because they have been resolved in other ways?

Mr Cassidy—Let us take it on notice. I think the tenor of what you are getting is that they are probably fairly few.

Senator BUSHBY—Thank you. Can the commission indicate how many cases it has commenced in relation to unconscionable conduct since last estimates? I know we have touched on this to some extent.

Mr Bezzi—Yes. I think we can do that. That was how many we have instituted, is it?

Senator BUSHBY—Yes.

Mr Bezzi—I do not think we have instituted any, Senator.

Senator BUSHBY—None.

CHAIR—Senator Bushby, I might go to Senator Abetz and Senator Milne now and come back to you.

Senator BUSHBY—They just whispered in my ear that I could go to 10 to and they would have five minutes each.

CHAIR—People always say they have five minutes but often creep over, depending on the length of the answers.

Senator BUSHBY—I will just finish these questions about unconscionable conduct. Does the commission consider unconscionable conduct a priority enforcement area?

Mr Samuel—I think I covered that in my opening statement, Senator, as to our position there.

Senator BUSHBY—Some of these have been asked already. Senator Joyce asked them. Can the commission indicate how many acquisitions it has considered in the grocery sector by reference to local markets since the last estimates?

Mr Cassidy—Again, Senator, it might be easiest if we take that on notice.

Mr Grimwade—Look, I think we will have to take that on notice. It would be a handful, I imagine, if not that.

Senator BUSHBY—I am happy for you to take that on notice because I get to ask another question. Does the commission consider that it lacks the power to review acquisitions in local markets, or do you have the tools you need?

Mr Samuel—This is a matter of some debate. Of course, you would be aware of some amendments that have been submitted to parliament in recent days in relation to that, Senator. We consider we have the power at present, but—I have to add this—there are some senior legal practitioners who have been contending to us that we do not have the power. The amendments that have been proposed I think are designed to remove those doubts.

Senator BUSHBY—That leaves that, so thank you very much.

Senator ABETZ—Thank you very much. I raise the issue of the King Island brand, the reliance on which is vital to King Island's economy and, therefore, social wellbeing. Does the ACCC have a view on the legality of products not produced on King Island bearing the brand name King Island? Is that deceptive conduct? Is it misleading conduct?

Mr Cassidy—Senator, this is something we have looked at in the context of complaints we have received. There are two issues. One is the actual King Island trademark, if you like, which is an approved trademark and which has certain conditions attaching to it. Basically, in order to use that trademark, those conditions need to be met. Indeed, if a product were to carry that trademark that had not met those conditions, they could potentially be in breach of the Trademarks Act or the Trade Practices Act for misleading and deceptive conduct.

The other related issue is a more generic claim of produced on King Island. This one is a bit trickier and came up particularly in relation to proposals to ship cattle off King Island and have them slaughtered and processed somewhere else. On our looking at that, our view was that if cattle had been basically born and bred and fed on King Island and all that happens is that they are taken off King Island to be slaughtered, we would be hard pressed to argue that someone could not say in relation to those cattle that they had been produced on King Island. Indeed, in the course of looking at that, we found there was a longstanding practice where a certain number of King Island cattle were actually being shipped to Tasmania and were being slaughtered and processed. For many years, it had quite happily been referred to as meat produced on King Island. So our view on that was that all that was happening was that the cattle were being slaughtered somewhere other than King Island, so it was probably legitimate for someone to refer to them as produced on King Island. But, moving away from that, if the cattle hypothetically were born on King Island but then spent most of their life somewhere else and someone was trying to claim it as being produced on King Island, that could well be misleading and deceptive in terms of the Trade Practices Act.

Senator ABETZ—I was at a restaurant up here not that long ago that had on its menu King Island chicken. Those of us that know King Island know that there are no chicken farms on King Island.

Senator BUSHBY—Or rabbits.

Senator ABETZ—Or rabbits, yes. But I will not take that point any further. Has your attention been drawn to the King Island *Courier* front page article of 19 May 2010 in which the King Island brand management group say they are struggling with ACCC ambiguity? From the article it seems as though you have been engaging with the group and providing information, if I might say, to the King Island *Courier* as well. You are responding to them. In the question, I want to compliment you for doing that because it would be very easy to try to ignore a relatively small and regional community and paper, so good on you for engaging with them. But that article did refer to ACCC ambiguities. Have you tried to assist the group to understand those ambiguities and get over those ambiguities? Have you confirmed that there are ambiguities in the laws that you have to administer that occasion some difficulty for you?

Mr Cassidy—Senator, I do not know which part of the question to take first. I think the ambiguities are probably the sorts of things I was just referring to about not having bright lines, if you like, around exactly what constitutes ‘produced on King Island’. We have been dealing with local people and entities on King Island in relation to the issue. I must confess that I am not aware of that particular article in the King Island *Courier*. But what we will do, if you can give us the article, is take the question on notice and perhaps give you a bit more detail about what is said in the article.

Senator ABETZ—Unfortunately, my time is up so I will not be able to ask you any questions about meat pricing on this occasion.

Senator MILNE—I want to raise matters in relation to the dairy industry in particular. You would be aware in the recent crisis that Tasmanian dairy farmers particularly allege that the ACCC has approved mergers in the processing side of the industry to the point where there is less competition and that the producers are being adversely impacted. Can you tell me whether the ACCC has done any review of this matter and whether the ACCC concedes that there is less competition in the dairy processing sector now than there was before the ACCC approved the merger, particularly in relation to National Foods?

Mr Grimwade—There seems to be some misconception—I was a witness at the dairy hearings—where I sought to explain that the commission did not holus-bolus approve the acquisition of Dairy Farmers by National Foods. I make the point that Dairy Farmers did not actually operate in Tasmania. The issues that we looked at were resolved through an 87B. Indeed, we would have opposed that matter but for receiving an 87B enforceable undertaking to divest a number of processors, a number of depots, distribution networks and brands to an essentially new competitor in particular regions, where we identified competition concerns. In particular, there was central New South Wales and South Australia. So we did have regard to competition concerns and act on those concerns in relation to that matter.

I also bring to your attention a more recent matter involving Murray Goulburn and Warrnambool Cheese and Butter Factory. You will be aware that we expressed some preliminary concerns in relation to that matter in a statement of issues we released I think around March. Today Murray Goulburn has advised that it is no longer pursuing that merger, so that matter has now been withdrawn from our purview.

Senator MILNE—Can you tell me if you are satisfied with the level of competition in the dairy processing sector in Tasmania?

Mr Grimwade—Well, in terms of merger review—

Senator MILNE—Or do you have concerns about it? Put it that way.

Mr Grimwade—There has not been a merger in Tasmania that we have reviewed for some time, so I cannot really answer the question as to whether the competitiveness of the sector is adequate, workable or not. In terms of our merger reviews, we look at the matter transaction by transaction. The last merger I think that we reviewed there was in 2006 and it related to National Foods’ acquisition of Lactos. There were a number of reasons that led us to clear that matter, not least of which was because Lactos, as I recall, operated in north-west Tasmania. National Foods was, I think, towards the south-east, where there was little overlap in the acquisition of milk from dairy farmers. There was also significant demand for milk,

particularly by Fonterra, at the time and in the foreseeable future that we identified at the time such that that matter did not breach the act, in our view.

Senator MILNE—In light of time, I want to ask about section 49 of the Trade Practices Act and the impact since its removal in particular on price discrimination. The dairy farmers argue, and the evidence given to the inquiry was, that a litre of fresh milk is the same whether it is in generic packaging or whether it is in a branded package provided we are talking about the same description of fresh milk. There is a whole variety of different milks, but let us assume we are talking about exactly the same fresh milk product. The farmers are arguing since the removal of section 49 you have a situation where there is a lack of competition in the processing sector, a duopoly in the supermarket sector and one contract from the supermarkets for fresh milk. The result is you have exactly the same products side by side in the supermarket. One is generic and one is branded. You have this situation where it is grossly unfair. How do you respond to that?

Mr Cassidy—I think before you arrived we had some discussion with Senator Joyce on price discrimination and the removal of section 49. Basically, what we said to Senator Joyce is that price discrimination is covered by section 46 of the act. But under 46 or, for that matter, the old 49, the fact that an identical product is priced differently is not in and of itself a breach of either section. You have to decide that there are anticompetitive consequences from that, so I think the short answer is removing 49 would not have had any impact, partly because the egregious conduct, if I can put it that way, still falls for consideration under section 46. But certainly it would not have had any impact because the sort of situation that you outline would not have been prohibited under the old section 49 anyway.

Senator MILNE—So what is your solution to the fact that the farmers would say very strongly that it does lead to adverse consequences for them? The supermarkets have the capacity where they offer one contract. Therefore, they can buy in bulk. Therefore, they can seriously discount exactly the same product to the detriment of the branded product to the detriment of the farmer.

Mr Cassidy—Senator, I think that is an issue that we probably cannot adequately deal with tonight. On the one hand, yes, there is, if you like, vigorous bargaining and competition for those Home Brand contracts. But, on the other, as I think we pointed out in the report we did on dairy, which was a number of years ago—in fact, when the National Foods contract was first put into place—that the reductions that were achieved by Woolworths through that contract were in fact, as best we could tell, passed on to consumers. So you have on the one hand a fairly what might be called vigorous tender process for what was a fairly lucrative contract, which drove the price down. On the other, the benefit of that, as best we could tell—we also looked at this in our recent grocery report—has been passed on to consumers.

Senator MILNE—The issue here, though, is that if farmers do not have a choice about who they can supply to, which they do not in southern Tasmania in the fresh milk market, they are stuck in this scenario and there is nothing they can do about it. What do we have to do to get a reference for the ACCC to look again at the level of competition in the dairy processing sector and, in particular, how that impacts on this issue of supermarket contract pricing and then generic pricing?

Mr Cassidy—That would really be a matter for the government, Senator. The grocery report, which we only completed in 2008, was by reference from the government. So it is really a matter for government.

Mr Pearson—I was at the same hearing with Mr Grimwade. We mentioned the fact that some 80 per cent of the milk in Victoria and Tasmania is actually processed. The price of that milk is generally driven by international prices. It is not driven by competition internally. Some of the price discrimination issues that were raised had to do with the fact that, in Victoria and Tasmania, the vast majority of their milk is for processed milk whereas in New South Wales and Queensland you are starting to look at drinking milk. I think drinking milk is about 25 per cent of the entire milk market. So when you start to look at the actual figures and percentages and try to determine what is driving the price of milk, you see that the international factors are huge.

I think in some of the figures we had then we showed that from 2001 to 2009 the Australian farm gate price increased by 30 per cent. Of course, nobody complained about that. Then with the financial crisis and with some of those massive issues that really hit on the international market, that is when all the problems and concerns arose in Tasmania. Some would argue that there is no discounting the fact that some of those farmers really suffered. We were well aware of that. But it was the international price. It was not a factor to do so much with domestic processing as with what happened in the international market. We have already had some press. I think there has been some noise already about the fact that Woolworths is splitting its contracts in Queensland. Already one of the issues that came out of the dairy inquiry was this notion of one contract. Woolworths are now splitting that contract. I think we have already seen some concerns raised by farmers. So it is a lot more complex than just saying, 'Split them' or 'Have more processes'. A lot of that is to do with the pressure from the international markets.

CHAIR—Thank you to the ACCC representatives for coming in this evening. The committee will now adjourn until 9 am tomorrow.

Committee adjourned at 9.00 pm