



## Competition Policy Review

### Joint submission by infrastructure owners and funders

Dear Professor Harper and members of the Review Panel

The signatories to this letter (**the Infrastructure Group**) each own (and in some cases operate) significant infrastructure assets in Australia. The Infrastructure Group welcomes the Competition Policy Review and looks forward to the broader debate around competition and industry policy that it will stimulate.

The liberalisation of government owned infrastructure – and opening up of related markets to competition – was a critical focus of the Hilmer Review and related reforms throughout the 1990s. This liberalisation and privatisation agenda was largely successful and, we believe, has contributed significantly to more efficient investment in infrastructure and related markets. This increased investment and competition has delivered substantial benefits to the users of infrastructure, and to Australian consumers generally. Infrastructure reform has promoted trade, improved competitiveness, reduced costs and resulted in better customer outcomes.

However, in part due to the success of those reforms, the context within which infrastructure now operates is markedly different, with many markets open to more competition and many utility assets privately owned and operated. The primary policy challenge is no longer the need to facilitate the efficient use of investment through the development and imposition of third party access regulation, but increasingly to attract efficient ongoing investment flows in new, existing and expanded capacity.

Consequently, it is important that competition policy reflects these changes by shifting the policy focus from regulatory intervention (to promote liberalisation) to instead ensuring regulatory *certainty*, *predictability* and an environment that *facilitates efficient investment* in new, expanded and upgraded infrastructure, including deregulation where competition has developed.

We believe that the Review presents a timely opportunity to reassess the regulation of infrastructure, from this viewpoint, and to ensure that the Hilmer policy objectives are appropriately adapted to drive investment and productivity.

#### **The priorities of infrastructure regulation need to evolve beyond Hilmer**

The important link between efficient investment in infrastructure and improved productivity is well established.

The combination of economic growth, population growth and the commodity super cycle have increased the demand for infrastructure capacity and for investment in new or expanded infrastructure, and there is a need to consider whether current regulatory approaches may at times be deterring rather than encouraging efficient investment. While recommending that the National Access Regime be retained, in 2013 the Productivity Commission nonetheless warned that:

Renewed emphasis should be given to ensuring that the Regime better targets the economic problem to reduce the risk of imposing unnecessary costs on the community and deterring investment in markets for infrastructure services for little gain.<sup>1</sup>

This is particularly the case since, while legacy infrastructure investment was once largely undertaken by governments, the majority of recent investment – the National Broadband Network being a rare and notable exception – has relied on private capital. This trend is expected to continue with the trend towards recycling of capital through superannuation funds investing in privatised State utility assets.

While governments may invest in infrastructure for a range of reasons, only some of which are economic, private investment will simply not occur without a settled expectation of a reasonable return on capital over the economic life of the asset and stable rules regarding recovery of the value of investments already made. Substantial costs (including opportunity costs) are incurred when infrastructure investment is delayed or deferred, both by customers and also by the overall economy.

The National Reform Agenda, and particularly the Competition and Infrastructure Reform Agreement (**CIRA**), provided an important acknowledgement by the Council of Australian Governments (**COAG**) that the economic objectives for competition policy have shifted substantially over the last two decades, particularly as they relate to key infrastructure. For example, the priorities under the CIRA are: to establish a simpler and consistent national approach to infrastructure regulation; to prefer access on the basis of commercial agreement rather than regulation; to prefer price monitoring to price regulation; to regulate access only where it will promote competition in upstream or downstream markets; and to make regulatory decisions within clear timeframes.

The Infrastructure Group endorses the direction reflected in the CIRA and makes the following recommendations to ensure that existing regulatory arrangements continue to adapt to new conditions (as markets are opened and become more competitive), to avoid inhibiting investment and flexibility in the way infrastructure is developed and operated, and to promote the development and growth of the Australian industries that depend on infrastructure services.

### **Only regulate infrastructure where it is necessary to do so**

The Infrastructure Group supports the Business Council of Australia's (**BCA**) criticism of the current "regulation impact statement" process as set out in its *Improving Australia's Regulatory System* paper and its recommendations that regulation impact statements should be mandatory for any significant new regulation and should be undertaken before the decision is made to proceed with that regulation. A disciplined and forward-looking approach to introducing regulatory intervention in markets is essential to encouraging much-needed investment in infrastructure.

Sectoral access regulation, in particular, should explicitly proceed on the basis that regulatory burdens need to be removed or reduced wherever possible, and intervention should be avoided unless it is clearly and unambiguously warranted. In this regard, the Infrastructure Group acknowledges the valuable contribution of the CIRA principle that terms and conditions for access to significant infrastructure should, in the first instance, be based on commercial negotiation.<sup>2</sup> This reflects the fact that direct engagement with customers is likely to lead to better customer outcomes, rather than relying on inflexible "one size fits all" regulatory solutions.

To deliver this kind of flexibility and customer-orientation, sectoral access regimes should contain explicit mechanisms to calibrate regulatory intervention to the minimum required to avoid the adverse exercise of monopoly power, and withdraw regulation where competition is effective.

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<sup>1</sup> *National Access Regime*, Productivity Commission Inquiry Report No. 66, 25 October 2013, p 10.

<sup>2</sup> Clause 2.2.

As an additional measure, there would be benefit in requiring all regulatory arrangements to define their objectives more transparently, and in implementing a process to ensure greater accountability in regulators' performance in pursuing those objectives, as discussed below.

### **Governments should provide regulatory certainty *prior* to investment**

With the focus in new access arrangements shifting from existing government-built assets towards privately funded or greenfield infrastructure, it is increasingly important that regulatory frameworks provide certainty to investors *before* they commit to an infrastructure project (either in the form of new greenfield investment or as part of privatisation processes). In assessing whether regulation is warranted, the Government should have regard to the overriding principle that light-handed regulation (and the removal of regulatory burdens, wherever possible) is preferable.

The Hilmer Review recognised the importance of certainty ahead of investment:

Accordingly, wherever possible the likely obligations to provide access should be made clear before an investment is made, whether that be through licensing requirements of a new facility or the acquisition of an asset formerly owned by government.<sup>3</sup>

The Infrastructure Group recommends that this concern be addressed through a clear and responsive process by which potential investors can fully understand the access arrangements to be applied to new infrastructure before being asked to commit their capital. Consistent with the general comments made by the BCA about the regulatory impact statement process in other areas of regulation, we believe that this should require governments across all infrastructure sectors to weigh the competitive benefits of regulated access against the risk that such regulation deters new investment in infrastructure, before taking any steps to impose or expand access obligations.

### **An Intergovernmental Charter of Economic Regulation**

The Infrastructure Group proposes that COAG establish an Intergovernmental Charter of Economic Regulation to guide the approach to the regulation of network industries. Among other things, the Charter would:

- require State Governments to clearly define “up front” their regulatory expectations around access (including issues such as expansion) as part of any privatisation process;
- require State, Territory and the Commonwealth governments and agencies to implement best practice features of access regimes, including clear objectives, established competition thresholds which determine the level of regulatory intervention appropriate, stable pricing and revenue principles, separation of the functions of access rule-making and regulation, and accountability mechanisms such as access to merits-based review;
- reinforce the CIRA principles regarding the desirability of reducing and simplifying the “regulatory footprint” in network industries and to prefer direct customer engagement wherever possible, over regulatory solutions unless these deliver clear and concrete economic benefits not available through commercially-agreed arrangements;
- require all sectoral regulators to develop, consult upon, and periodically publish a strategy document setting out clear guidelines as to the circumstances in which the regulator will and will not intervene in a market in relation to which it already has regulatory powers, and on how it plans to reduce regulatory burdens in the market over time, in order to provide transparency and certainty for industry; and

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<sup>3</sup> Page 251.

- require regulators' performance to be independently assessed periodically against these guidelines by an independent authority (e.g. in accordance with the Productivity Commission's *Regulator Audit Framework*, March 2014, and the Australian National Audit Office's *Administering Regulation Better Practice Guide*, June 2014).

The Infrastructure Group points to experience in the United Kingdom, where the United Kingdom's Department for Business Innovation and Skills has put in place strategy and policy statements for regulators in each regulated sector to establish context and guidance about their priorities and desired regulatory outcomes (Principles for Economic Regulation).

The United Kingdom's regulators have responded to this guidance by providing clear and detailed annual statements of their objectives and planned actions, which in turn have given industry participants increased certainty and greater involvement in regulatory priorities.

## **Conclusion**

In summary, the Infrastructure Group considers that:

- the focus on access regulation aimed at supporting the liberalisation processes of the 1990s is no longer the most urgent focus of infrastructure regulation, given that this process has largely been completed and has been overtaken by a need for increased capacity;
- looking forward, the regulation of infrastructure should have as its objective the facilitation of investment by limiting regulatory intervention to dealing with issues where direct customer engagement and agreement between network owners and customers is not possible;
- lower costs and better customer outcomes will be best served by providing greater "up front" certainty for investors, including defining the Government's regulatory expectations before any capital is committed and then ensuring stability over time that reflects the long economic lives of the infrastructure which is required to provide these services; and
- improved accountability of regulatory processes should be delivered by publishing periodic strategic guidance to regulators (and making their performance against this guidance subject to independent assessment).

The Infrastructure Group would welcome the opportunity to meet with the Panel to discuss these submissions in more detail.