



ACCI's Revised Infrastructure Policy

Infrastructure is made up of the basic facilities, services and installations needed for the functioning of an economy, including telecommunications, transport networks, electricity, gas, water, hospitals and schools. It is essential that our infrastructure is sufficient to facilitate sustained and robust economic growth and improve Australia's economic performance. At ACCI's December General Council meeting, we adopted a revised infrastructure policy which is reproduced in this article.

In summary, ACCI's policy argues that:

- infrastructure needs should be primarily addressed by the private sector, because it is generally more efficient at developing and operating infrastructure. The Government should assist private investment through facilitative tax and regulatory systems;
- government investment should only be used when there is clear and demonstrated market failure and after a thorough cost benefit analysis has been undertaken. Where government involvement in infrastructure is required, governments should make full use of partnerships with the private sector to reduce costs;
- consistent with proposals to reduce business regulation, the regulations applying to infrastructure planning, development and use should be examined and removed if they do not meet cost-benefit tests;
- ACCI does not support proposals to have a national takeover of infrastructure investment decisions. States retain an important role. However, we do support proposals for greater coordination in infrastructure regulation and planning.

POLICY OBJECTIVES

ACCI's major policy objectives in regard to infrastructure are:

- to advocate continuous improvement of infrastructure;
- to encourage technological change in all areas related to infrastructure;

- to ensure that the private sector has a major role to play in financing, designing, building, operating and maintaining infrastructure;
- to remove legislative and taxation obstacles to increased private sector infrastructure activity;
- to ensure that all infrastructure projects are subject to a proper cost-benefit analysis which takes into consideration all economic, social and environmental considerations. Public spending on infrastructure should ensure the maintenance of fiscal responsibility; and
- to make certain that equitable and sustainable risk allocation models are developed for each project undertaken by the private sector.

THE POLICY FRAMEWORK

Importance of Infrastructure Development

Infrastructure is vital to Australia. It is essential to:

- improving Australia's economic performance;
- maintaining and enhancing our international competitiveness;
- education and training;
- national security;
- social cohesion; and
- enhancing our built and natural environment, taking into account the environment in which we live.

Traditional Public Sector Role

Historically, most infrastructure has been provided by the public sector.

The main reasons for this traditional reliance upon government to provide infrastructure are:

- infrastructure has been seen as essential for economic activity, so government has been expected to guarantee its development;
- infrastructure is generally large scale, requiring large outlays of capital;
- infrastructure developments are often natural monopolies meaning there is seldom an opportunity for more than a single provider to survive;

- infrastructure is often ‘non excludable’, so that it is difficult to exclude someone from using it, for example, national defence. Accordingly, it is often difficult for the provider to recover all of the costs involved through the sale of services;
- infrastructure often generates social benefits greater than the private benefits accruing to its direct consumers, such as the general improvement in community welfare generated by a higher enrolment in educational institutions (these benefits are also known as externalities). Accordingly, it has been considered that there is likely to be underprovision of such infrastructure if the provision of infrastructure is left entirely to the private sector;
- provision of infrastructure is often politically sensitive in that governments are held accountable for prices charged and service outcomes; and
- infrastructure projects can require government intervention and legislative changes to allow successful completion of projects.

Problems with Public Sector Provision of Infrastructure

While the public sector has traditionally been the main provider of infrastructure, there are a number of potential problems with public sector provision.

This “government failure” may be overcome with a greater reliance on private sector provision.

- Government investment requires costly taxation to finance. Higher taxes increase efficiency costs (deadweight losses), encourage tax avoidance and evasion and can have high compliance and administration costs.
- The private sector is more responsive to market needs, because it has to make a profit.
- Private sector construction, development and operation is usually more efficient than government sector.
- The private sector can bring greater expertise, experience and innovation.
- Government investment can be swayed by political considerations, meaning investment can be very inefficient.
- Governments frequently undercharge for infrastructure use. This is inefficient, causes congestion and overuse of the infrastructure and can be environmentally unfriendly.
- Governments may have political constraints on their ability to finance some worthwhile investments (particularly large ones).

- Government involvement in infrastructure can mean underinvestment in the longer term. Those sectors where the capital stock is most deficient are those where governments remain the dominant suppliers.¹
- Government investment in sectors with infrastructure deficiencies “risks creating perverse incentives by rewarding incompetence. A far better approach would be to identify and remove the regulatory, policy or other failings which caused the bottleneck to arise in the first place.”² It also implicitly penalises sectors where infrastructure is better managed.

Rebuttal of Arguments Against Private Provision of Infrastructure

The main concerns with private sector investment are generally not valid. Some issues raised and ACCI’s responses are outlined below.

- *Private infrastructure requires a return, so charging for use is required.* While this is true, government investment requires taxation – which can often be less efficient than charging those who use the infrastructure more directly. It can also be inequitable for all Australians to pay for infrastructure that is used by a fraction of the population.
- *It is administratively difficult to charge for infrastructure use.* While this is true for local roads, it is generally not true for any other type of infrastructure. In addition, difficulties with user charging are diminishing over time with new technologies. In comparison, the compliance and administration costs of taxes can be substantial.
- *The private sector does not take account of positive externalities from infrastructure investment.* However, any private sector investment that is profitable provides a benefit to the economy as a whole, and the difference between infrastructure and other investment in this area is not very clear. Furthermore, this market failure argument ignores the risk of government failure, as outlined previously. Nevertheless, if positive externalities are clearly an issue, the best response is government subsidies to the private sector, rather than the government taking on all the investment.
- *The Government can borrow at lower interest rates than the private sector.* While this is usually true, government borrowings need to be repaid from taxes which have high economic costs. When this is taken into account, the cost of public borrowing is likely to be higher than private sector borrowing.
- *The private sector will overcharge for the use of monopoly assets.* This problem can be addressed by proper price regulation (see below).

This is not to say that governments should never invest.

Government investment can and should occur when there is a clear and demonstrable market failure that outweighs any potential government failure and after a thorough cost benefit analysis has been undertaken.

Even in this case, partnerships with the private sector should be used to reduce development and operating costs (see section on revised public role below).

Technological and Economic Change Fostering Private Sector Involvement

As mentioned, it is increasingly apparent that there are potential problems with government provision of infrastructure that may be overcome with a greater reliance on private sector provision.

There is now far greater scope for private sector provision of infrastructure.

Market forces can be harnessed to a far larger extent and the development of modern technologies has allowed the introduction of competition into monopoly infrastructure markets. Contracting out has become more commonplace. Privatisation has become increasingly acceptable and there is greater public acceptance of the role of the private sector in the provision of infrastructure.

In addition, Australians are becoming more familiar with the concept of ‘user pays’ and hence, more accepting of tolling and other direct charges for service previously provided free to users. This change in community attitudes has allowed governments to engage the private sector in infrastructure development that may not otherwise have occurred.

Revised Public Sector Role in Infrastructure Provision

As the private sector assumes an increasing role in infrastructure provision, governments must revise their role in this process, moving from traditional supplier to consumer and funding provider.

There is an ongoing role for government in developing a positive environment for efficient and effective infrastructure investment.

The general state of the economy is very important – and continuing economic reforms (as advocated by ACCI) are essential to ensure that the economy can pay for infrastructure investment.

Particularly important are workplace relations reform, competition policy, tax reform and training.

Government, in conjunction with the private sector, should implement processes which identify strategic opportunities and weak links in the economy to encourage further private investment.

In particular, the Government should ask a suitable body (such as the Productivity Commission) to conduct regular reviews of infrastructure needs and the barriers to meeting these needs.

Private sector involvement will only materialise if projects are commercially viable, or through subsidies to private sector providers, so that they become profitable.

Therefore, arguments can be made for establishing public-private partnerships (PPPs) to design policy initiatives to best meet the needs of business and communities.

For PPPs, Governments should make certain that equitable and sustainable risk management strategies are developed for each project and that risk is shared and allocated between the parties on the basis that it is manageable and ensures the long term sustainability of the project and its participants.

There needs to be an open and transparent process for government assistance to private sector infrastructure development which makes it clear where subsidies, grants, taxation agreements and other forms of public assistance have been provided.

The Australian Government has recognised the difficulties associated with attracting domestic and foreign investment within Australia and as part of its business tax reform program is promoting venture capital investments in Australia.

Section 51AD and Division 16D of the Income Tax Assessment Act impede investment in infrastructure. These provisions remove tax benefits to investors providing property to tax exempt entities such as governments.

They were implemented in a period before private provision of public infrastructure was generally contemplated. These provisions should be reformed, as they are no longer appropriate measures to prevent tax avoidance and can jeopardise joint public-private sector infrastructure ventures.

To ensure that economic activity is not constrained unduly by lack of sufficient infrastructure, governments must ensure they plan adequately for future needs and fund these sufficiently. Therefore, it would assist if the current bias in public sector spending towards recurrent expenditure rather than capital expenditure was reversed.

Governments can and should invest in infrastructure when the private sector cannot. However, any infrastructure proposal that involves outlays of public funds should be subjected to a properly conducted cost-benefit analysis which looks at the net economic, social and environmental benefits of any particular project. Proper costing and recognition of alternate uses for resources must remain major aspects of such analyses.

Privatisation of Infrastructure

Existing government-owned infrastructure can be sold (i.e. privatised). As argued elsewhere in this policy, private operators are more likely to increase operational efficiency, increase productive investment, reduce unproductive spending and provide what the markets want (rather than what is politically expedient).

Privatisation is likely to provide the greatest benefits when:

- the infrastructure operates in more competitive markets, or is not a monopoly;
- the government has a conflict of interest between being an infrastructure owner and a regulator; or
- the government-owned assets may be competing unfairly with the private sector.

The decision to privatise should not be driven by the amount of money raised by privatisation, although the government should ensure it receives a fair price.

If a monopoly is privatised, regulation of pricing and service standards is needed to ensure that the private owner cannot abuse its market power.

Regulation of infrastructure

Regulation of Investment

Federal, state and local governments regulate building and investment. These regulations have a substantial impact on infrastructure, which can occupy large areas of land.

These regulations can make infrastructure development difficult and costly.

For example, concerns have been raised that the restrictions on port operations and expansion can be onerous. Nearby residents complain of constant noise and can demand restrictions on operations or investment.

While these regulations can provide important social benefits, ACCI believes that these benefits should be weighed against the costs that are imposed on business. Regulation should only occur when the benefits clearly outweigh the costs.

If a regulatory response is required, the regulations should be designed in consultation with industry stakeholders to minimise costs while maximising benefits. Regulatory decisions should be made in a timely fashion and governments should provide adequate resources to regulators so that this can occur.

Regulation of Pricing

ACCI supports the National Access Regime, which provides third party access to essential infrastructure as this will increase overall economic efficiency.

The National Access Regime should be focused primarily on improving access to these essential facilities which are not commercially or economically viable to replicate.

However, it should not provide a means for a potential competitor to gain access to the capital assets of a provider simply because it would be commercially convenient.

The regulator for the Access Regime should be limited to arbitration when an access provider and a potential user cannot reach agreement. More broadly, the emphasis should be on encouraging agreement without the interference of a third party.

The regulator should not have the power to overrule a market agreement, simply because it believes that the agreement is unfair.

ACCI does not have a preference for any particular access pricing method, but the method:

- should not be at an unreasonable cost to the owner;
- should take account of maintenance costs and the efficient cost of capital; and
- should not discourage future investment or research and development.

Infrastructure should only be declared to be subject to the Access Regime if it is likely to create a substantial increase in competition.

Government-owned assets should be fully subject to the Access Regime. This will ensure consistency with competitive neutrality principles.

Government involvement in decisions should be minimised and government should only overrule decisions for reasons of national interest, not sectional or political interest.

National Infrastructure Coordination

ACCI does not support proposals for a National Infrastructure Council, or similar, to take over decision making on infrastructure projects.

As argued elsewhere in this policy, the private sector should be the primary focus of investment.

ACCI is concerned that such a Council will:

- dissolve into arguments between sectors or jurisdictions over who deserves more money;
- support government spending over the private sector; and
- support projects that have poor returns.

We do however support proposals for coordination of infrastructure regulation decisions. Infrastructure regulation should be an issue for regular discussion at the Council of Australian Governments (COAG).

We are supportive of recent increases in national coordination of regulation, particularly for water (through the National Water Commission) and electricity (through the Australian Energy Regulator).

END NOTES

¹ AusCID (2005) Submission to Exports and Infrastructure (Fisher) Taskforce, p9.

² CCIWA (2005) Submission to Exports and Infrastructure (Fisher) Taskforce, p1.