IS THERE A CASE FOR STATE STATUTORY MARKETING ARRANGEMENTS?[1]

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1. Introduction

The issue of State statutory marketing arrangements (SMAs) is discussed from the practical perspective of setting State Government policy. Should the State maintain legislation to give effect to a statutory marketing arrangement? Should the SMA be subject to the Commonwealth Trade Practices Act (TP Act)? To what extent should operating guidelines and procedures resemble those of private sector businesses?

The case developed in this paper has three main elements to it:

(i) States should maintain legislation to be able to give effect to SMAs.

(ii) Procedures for establishing and reviewing SMAs should be significantly different to the present situation, at least in NSW.

(iii) Operating guidelines for SMAs should be significantly different also.

2. Market Failure, Economic Efficiency, The Trade Practices Act and SMAs.

The case for SMAs has generally been based on an alleged 'market failure'. Examples include countervailing the market power of middlemen, controlling the market supply of commodities whose production is markedly influenced by season, and meeting social objectives such as the security of food supply.

The last mentioned example serves to highlight that social attitudes and values are significant to this topic of SMAs and that these attitudes do change. Stability and security of domestic food supply are no longer significant issues.

Today, no challenge is issued to the principle that economic efficiency (social welfare) considerations should significantly influence decisions on any future grant of statutory marketing powers. Issues in the application of this principle include the particular test, the methodology of analysis and the decision process that follows an economic analysis.

The application of economic efficiency criteria to marketing arrangements has been written into legislation in the (Commonwealth) Trade Practices Act (TP Act). Given the existence of the TP Act as a means by which various 'market failures' might be

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overcome, it is pertinent to ask why State statutory marketing legislation should be needed for the same purpose?

If State Statutory marketing legislation is to be justified in addition to the TP Act, then either or both of two conditions should be met. These conditions are:

(i) that the TP Act is unable to give effect to some market arrangements that can meet economic efficiency conditions; and

(ii) that the 'costs of compliance' with TP Act procedures and regulations are too high relative to the applicants' ability to pay and/or to the costs of market failure.

These same conditions are also reason to change the TP Act. Therefore, reason to maintain State statutory marketing legislation relies on a further judgement that such conditions are likely to recur.

To give full economic justification to State statutory marketing legislation, it is also necessary to take account of the social (taxpayer) costs of maintaining the legislation and established arrangements.

1.1 The Trade Practices Act : Possible Imperfections

There are a number of deficiencies in the TP Act from the point of view of a consistent application of an economic efficiency criterion. In its Report on Statutory Marketing Arrangements, the Industry Commission (1991) recommended change only in relation to the blanket prohibition on authorising voluntary recommended price agreements between fewer than 50 parties[3]. A much more in-depth critique of the TP Act has since been developed by the Industry Commission in its discussion paper on Pro-competitive Regulation[4].

Other deficiencies of the TP Act include:

(i) the blanket prohibition on some anti-competitive behaviours regardless of whether public benefit can be demonstrated.

(ii) the market dominance test of mergers while established monopolies are permitted to continue.

Reservations have also been expressed about the criteria, methodology and decision-making responsibility established under the TP Act. For example, the Centre for International Economics expressed the following viewpoints:

* "One reservation we have concerns the TPC's apparent assumption that

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[3] Industry Commission (1991) Statutory Marketing Arrangements for Primary Products. Report No. 10 (26 March) p. 107

[4] Industry Commission (1992) Pro-competitive Regulation. Discussion Paper.

decisions made by government through the political process are inferior to decisions made by the TPC."[5]

* "The question is whether decisions made by an elected government, which although they may appear to be a matter of 'whim', are inferior to decisions made by the TPC. Moreover, it is not as if the decisions that the TPC would come to are technical so that each case would have one and only one answer; considerable discretion seems inevitable."[5]

* "A reservation which might be raised about the authorisation track is that once the TPC makes its decision it becomes law. This approach may be contrasted with the IAC type review process, which is advisory and leaves questions of legislation to the government. The authorisation process appears to be one that changes legislation by a regulatory body. Whether this would result in more or less 'regulation' is a moot point."[5]

The possibility of using different tests was noted by the Law Reform Commission of Victoria in a discussion paper on restrictive trade practices legislation[6]. For example, consumer benefit might be specified in preference to public benefit.

Methodology of analysis was raised by the Industry Commission which noted "some concern that the criteria used by the TPC to assess public benefit may be rather narrow."[7] The TPC responded in a determination released shortly afterwards "the Industry Commission was concerned that public benefit should be given a wide interpretation in relation to the operations of statutory marketing bodies which accords with the Trade Practices Tribunal's and the Commission's view of public benefit."[8]

The situation of the Trade Practices Commission is compounded by its roles of both analyst and decision maker. Nonetheless, the foregoing comments reflect some debate about the related issues of whether analyses should be purely quantitative and the extent to which subsequent decisions should include a qualitative element that takes account of unquantified considerations.

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5 Centre for International Economics (1990). Assessment of the Impact of Trade Practices Legislation on NSW Agricultural Marketing Boards. p. 49

6 Law Reform Commission of Victoria (1991). Competitive Law: The Introduction of Restrictive Trade Practices Legislation in Victoria. p. 13

7 Industry Commission (1991). Ibid. p. 105

8 Trade Practices Commission (1991). Determination: Application for Authorisation Registration No. A30138. File No. CA90/4 (28 June).

1.2 The Trade Practices Act : Costs of Compliance[9]

The TP Act imposes a significant cost on applicants. Imposition arises from the 'guilty until proven innocent' basis of the Act. Costs have two key elements - th' cost of applying to the TPC for authorisation and the costs of appealing to the T' should authorisation not be granted by the Commission.

The costs of an application to the TPC are raised by the Commission's requirement that applicants provide "independent audited estimates" of claimed benefits. The significance of this requirement was recently noted by the Commission:

"...The Commission had a heavy duty to ensure that the public benefit outweighed the anticompetitive detriment. ... It was Commission policy in authorisation applications to call for audited or independent estimates."[10]

"...He (Professor Round) said the Commission appreciated that it was expensive for smaller companies to provide that information but, if the Commission has to assess this material, it may not give as high a weight as possible to figures if audited estimates have not been provided. He said it did not mean that the Commission would ignore them but it would put a question mark over those estimates, where they were provided by the companies concerned, if such figures were unsupported."[11]

The costs of an appeal to the TPT result from the legal nature of the appeal and the process of (information) discovery that is part of an appeal.

The costs associated with the application of the TP Act were recently commented upon by the Industry Commission:

"...the administrative approach also imposes significant costs. Costs may result from the ad hoc nature of TPC activities, the possible divergence of views between the TPC and the judiciary because of the limited role of litigation in the interpretation of important provisions, and uncertainty resulting from the judicial power to overturn any administrative decision.

Further, the costs of judicial enforcement may be higher than necessary for a range of reasons. For example, evidence on market power must be compiled in a more protracted and expensive way because of the rules on the admissibility of evidence in restrictive trade practices cases. Other reasons for the excessive costs of

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[9] Other areas of regulation are significant to a more complete discussion of compliance costs as they relate to the SMA issue. A particular issue is the relative costs of establishing a company or co-operative. SMAs follow the co-operative model for which significant assistance in making establishment arrangements is provided by government.

[10] Trade Practices Commission (1991) Record of Pre-Decision Conference in relation to an Application for Authorisation on behalf of Macadamia Processing Company Limited and Suncost Gold Pty Ltd p. 4

[11] Ibid p. 5

judicial enforcement include a lack of competition in the provision of legal services."[12]

For those who subscribe to a game theory approach to human behaviour, the potential cost of an appeal to the TPT, and the likelihood that an appeal option will not be exercised, raises a further issue of concern. That issue is the possibility that the TPC might use the situation not simply to administer an economic law but to give effect to a broader array of government policies that might fall within the umbrella of microeconomic reform.

Notably, the Commission associates itself with such a broader role:

"The Commission will increasingly examine the reach of the Act, consistent with the Government's stated policy:

> The benefits for the consumer of expanding the scope of the Trade Practices Act could be immense... This has to be done
> *Building a Competitive Australia*, 12 March 1991"[13]

1.3 Relating Trade Practices and Statutory Marketing Legislation

Discussion so far carries the implication that States should maintain legislation to be able to give effect to statutory marketing arrangements. This raises the question of what exemption, if any, the SMAs should have from the TP Act.

Earlier comment was to the effect that there should be marked change to current procedures for SMA establishment. A public benefit assessment should significantly influence any establishment decision.

Accordingly, and as the general rule, it would be appropriate for a proposed SMA to be referred to the TPC for authorisation in its establishment process. This action would not only be consistent with a common application of competition law but also have the further advantage of paving the way to full privatisation should the authority move to do so.

However, because of problems such as have been commented upon, it will also be appropriate to allow the possibility of SMA establishment without referral to the TPC. A State Government decision to proceed without authorisation could be challenged by the TPC if it saw fit to do so. The TPC does have this option at present[14] although its non-use of this option to date must be seen as an issue in Commonwealth-State relations more so than in terms of law.

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[12] Industry Commission (1992) Pro-competitive Regulation. Discussion Paper p. 101

[13] Trade Practices Commission (1992) Priorities for 1992 & 1993 p. 2

[14] Commonwealth Department of Primary Industry (1985). The Trade Practices Act and Primary Industry. p. 6

2. Availability of Statutory Marketing Powers

Assuming a continuation of SMAs, an important issue is how to limit the statutory powers they can access. One way of limiting access is to ban (not make available) certain powers but this approach runs the risk of introducing a problem of the same nature as has been noted in relation to the TP Act. That is, an arrangement could not be established even if a public benefit was demonstrable.

To ban access to certain statutory powers requires prior definition of the powers that are acceptable and those that are unacceptable. It appears that CIE may have had such an approach in mind when developing its spectrum of marketing authorities functions.[15] However, its work did not go as far as suggesting which powers should and should not be accessible.

When making its submission to the Industry Commission inquiry on SMAs, the NSW Government attempted to define what grounds there are for Government intervention in the marketplace.

"The answer lies in only a relatively limited set of circumstances where:

- intervention may improve market efficiency where there is a "free rider" problem (such as in the areas of generic product promotion, and the development of standards and quality assurance programs),

  or

- there are opportunities for maximising export income through possible premiums resulting from single desk selling.

In principle, the NSW Government does not favour granting compulsory acquisition or vesting powers to State based producer organisations unless either of the above two conditions are satisfied."

Even these issues of overcoming a free-rider problem and single-desk export selling are not clear cut. There can be opposition to the free-rider argument on the grounds of denial of an individual's rights. Some opposition to single desk selling relates to the lack of competition in supplying services in product and market development.

An approach to this problem issue of granting statutory powers has the following three elements.

(a) A grant of any statutory powers should be the subject of a public benefit assessment and a process of informing the public of the assessment.

(b) The petitioning process for the establishment of an SMA should begin with a petition for statutory powers to pursue specified objectives. This approach is

[15] Centre for International Economics ibid. p. 144

in contrast to the current situation with the MPP Act in NSW whereby growers effectively petition to establish an organisational structure. The merits of separating objective, power and structure, and assessing them in that order was also commented upon by the Industry Commission.[16]

(c) In the case of vesting power in particular, some guidelines might be given as to how it may and may not be used. The establishment of a statutory Consultative Committee for the NSW Grains Board may be interpreted as a step in this direction.

3 Accountability and Related Matters

A reassessment of concepts and procedures on accountability has driven much of the recent change to SMAs, particularly at Commonwealth level. Newton[17] outlined the chain of developments which link back to the 1976 Royal Commission on Australian Government Administration.

Key issues are:

(1) to recognise accountability as a purposeful and directional concept [ie. account to whom for what].

(2) to recognise an inverse relationship between accountability and autonomy [ie. the more accountable an SMA is to Parliament, the less autonomy it has in decision making].

When these concepts are set in the context of an SMA that is financed by growers and is primarily for the benefit of growers, significant change is implied for many of the traditional arrangements relating to the structure and operation of an SMA.

With specific reference to accountability, it is necessary to consider at least three relationships:

* Minister and Parliament to public
* Board of Directors of SMA to Minister
* Board of Directors of SMA to grower shareholders

Given the changing thinking about SMAs, financial accountability should primarily be expressed in the relationship between a board of directors and growers. This assumes no real or potential financial input to the SMA from government.

Accountability of the SMA to Parliament should then centre primarily on the SMAs use of statutory powers and whether it is operating in accordance will the powers granted.

Through a public hearing process prior to establishing a SMA or renewing a grant

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[16] Industry Commission ibid. p. 140

[17] Newton, A (1988), Innovations in the Administration of Primary Industry Statutory Authorities, paper presented to the International Symposium on Australian Public Sector Management and Organisation, Brisbane (7-8 July).

of statutory powers, Parliament accounts to the public for its decision.

In conjunction with this changed thinking an accountability there must be consideration of the array of issues such as were considered by the Davis Committee.[18] Suffice it to say that the SMA must become a marketing specific, commercially oriented organisation.

4 Discussion and Conclusions

The question of State SMAs is complex. Their establishment and continuation should be subject to economic efficiency considerations. Given the existence of the Trade Practices Act, it may be argued that State legislation to establish SMAs is theoretically unnecessary.

However, there are problems involved in regulating the application of theory. These difficulties are associated partly with the task of writing economic theory into economic law and partly with the task of writing on economic law that can accommodate change in the economy and society to which it applies.

The difficulty of the situation is reflected in the following findings of the Industry Commission:

- "Many features of statutory marketing arrangements – especially those dependent on powers of acquisition, production control and pricing – adversely affect the efficiency of resource use."[19]

- "Many objectives of statutory marketing arrangements are sound from the viewpoints of both producers and the wider community."[20]

Given problems such as have been discussed in this paper, it is appropriate for State Governments to maintain legislation to give effect to SMAs. However, the legislation should be significantly different to that which exists, at least in NSW.

Desirable characteristics of statutory marketing legislation would include:

- SMAs to be established for commercially oriented purposes only.
- Petitions for the establishment of SMAs to be in terms of a request for statutory powers to pursue stated objectives (rather than to simply establish a structure).

[18] Review of Commonwealth Primary Industry Statutory Marketing Authorities. Ibid.

[19] Industry Commission (1991) Statutory Marketing Arrangements for Primary Products. Report No. 10 (26 March) p. 4

[20] Ibid. p. 2

- Proposed arrangements to be subject to an economic efficiency assessment. [Objective, power and structure would all be examined].
- Ministerial decision to allow a poll for SMA establishment would be influenced by the economic efficiency assessment.
- SMAs should be sunsetted [continuation beyond a fixed term should be subject to review and reestablishment].
- Organisational characteristics of SMAs should be based on an appropriate corporate model; the model may be different for different SMAs.
- SMAs should have a right to fail without any real or implied financial assistance from government.
- The accountability relationship between a Board of Directors of an SMA and its grower "shareholders" should be strengthened.
- While SMAs will gain increased autonomy from government, it will be appropriate for government to retain a veto power of approval over a number of SMA actions.

It is reasonable to anticipate some reduction in SMAs as a result of these changes. Whether the change will lead to a demise of SMAs that operate on the domestic market - as was implied by the Davis Committee in relation to the Commonwealth SMAs[21], and as was noted by Johnson et al.[22] as a result of deregulation in New Zealand - is a debatable point. A Californian study by French and Nuckton would suggest not necessarily so.

French and Nuckton reviewed a Californian marketing order (price stabilisation through volume control) with a 40 year history and concluded: "Overall the results of the study suggest that public interest may have been well served by the raisin volume control program, or at worst, there was no significant welfare loss."[23]

[21] Review of Commonwealth Primary Industry Statutory Marketing Authorities (Professor J G Davis, Chairman) (1990), Report to the Minister for Primary Industries and Energy by the Review Committee, AGPS, Canberra.

[22] Johnson, R W M, Schroder, W R, and Taylor, N W (1989). Deregulation and the New Zealand Agricultural Sector: A Review. Review of Marketing and Agricultural Economics 57(1-3):68

[23] French, B C, and Nuckton, C F (1991). An Empirical Analysis of Economic Performance under the Marketing Order for Raisins. American Journal of Agricultural Economics (August), p. 593