

COAG MEETING: 3 JUNE 2005

A NEW GENERATION OF REFORM – PROSPERITY, PRODUCTIVITY AND PARTICIPATION

1. GOVERNMENTS WORKING TOGETHER

Australia has been transformed over the past 20 years as governments have pursued sustained economic and social policy reform.

The COAG agreement of ten years ago to implement National Competition Policy (NCP) was a key part of this reform. These measures were pivotal in boosting the competitiveness and growth of the Australian economy. That agreement shows what can happen when Commonwealth, State and Territory Governments have a common purpose and collaborate to implement major reforms.

The dismantling of over protected and institutionalised economic structures has seen the nation enjoy an unprecedented run of growth and prosperity.

The dividend to Australians in terms of employment, income, wealth creation and government services has been great.

However, these improvements in our quality of life are under threat as national demographic trends begin to bite and global competition intensifies.

An ageing population, slowing productivity growth and weak non-mineral export performance are signals that a second wave of reform is required to sustain and grow the good work already undertaken.

Our future prosperity will depend on the ability of all Governments - Commonwealth, State and Territory - to embrace reform that addresses the key areas of participation and productivity.

Preliminary Victorian estimates suggest that a refreshed reform agenda that achieves a 1.5 percent lift in labour productivity over the next decade, and a 2.7 percentage point increase in labour force participation, would potentially add 5.6 percent to aggregate GDP by 2015.

The effect on government revenues and expenses would also be considerable. It is estimated that the Commonwealth Government would gain about \$9.4 billion in its operating balance, having passed on its increased GST revenue. The States and Territories would share a more modest \$3.4 billion in increased operating balances, having received the increased GST payments.

The reforms pursued over the past decade under the framework of NCP have proven the ability of governments to cooperate effectively in the national interest.

The challenges facing Australia over the next decade are no less significant. They are structurally based and a sustained and cooperative effort is again required to meet them.

Victoria urges the Commonwealth, States and Territories to embrace a new generation of collaborative reform as outlined in this Communiqué.

1.1 THE ACHIEVEMENTS OF NATIONAL COMPETITION POLICY

A collaborative national approach was the cornerstone of successful implementation of the NCP reform agenda. It drew together the reform priorities of the Commonwealth, States and Territories, to improve Australia's overall competitiveness and raise living standards – with Australian income per head rising from 17th in the OECD in 1990 to 10th in 2003.

Effective governance arrangements have been a critical part of NCP's cooperative approach, through which States and Territories were paid dividends in return for their contributions to national reform initiatives.

While the benefits of NCP reforms are significant, gains from a broader economic and social policy reform agenda have the capacity to deliver much more to the community. Collaborative action on issues of national importance is again required, as a fragmented reform agenda will not achieve the momentum and commitment required for sustainable reform.

1.2 REFORMS MUST CONTINUE

It is important not to be complacent about the continued performance of the Australian economy. Resting on the achievements of the last decade will cost the Australian community opportunities for greater prosperity.

Australia's productivity performance is under threat, with further reform essential if the economic expansion of the last 14 years is to continue. There remains potential for labour force participation rates to improve to match leading OECD nations.

The Australian economy is operating in an intensely competitive international environment. As a small trading nation, Australia will drive its economic growth by minimising barriers to trade and maximising its business flexibility. However, there are signs that infrastructure constraints could limit growth of Australia's export volumes. Education and training systems are not keeping pace with the educational requirements of a successful international economy.

By addressing these issues through a national reform effort, the future outlook is positive. Introducing reforms to steadily increase labour productivity by 0.15 percentage points per annum over the next 10 years will mean that by 2015, labour productivity would be 1.5 per cent higher. This will lead to a potential additional improvement in Australia's GDP of 1.4 per cent by 2015.

Reforms to increase participation rates by an additional 2.7 percentage points will lift GDP an additional 4.2 percent.

These productivity and participation-based reforms would enhance Australia's international competitiveness and by 2015 result in a net increase in export volumes of approximately 10 per cent.

Over this time the ageing of Australia's population along with rising costs of health care will be causing significant budgetary pressure. This would be ameliorated by the effect of this new reform agenda on participation, productivity and as a result on governments' budgetary positions.

The case for continuing reforms on a collaborative basis has never been clearer.

1.3 PRINCIPLES FOR REFORM

This new reform agenda is both challenging and exciting. It involves all levels of government guided by key principles.

Collaborative federalism will see the Commonwealth, States and Territories pursuing a shared vision to deliver economy-wide benefits, with each jurisdiction determining the means to achieve continuous improvement.

Reforms will be expanded to include social policy initiatives. Competition policy-based reform will be only one component of the new reform agenda.

Economic and social reforms will occur where there is a clear net benefit to the community. Inevitably, additional government expenditure on health, education and training will be required. It also is desirable that the distribution of potential benefits, and adjustment mechanisms, are considered when designing reform initiatives.

Under a genuine and equal partnership between the Commonwealth, State and Territory Governments, the reform agenda, timeframes, assessment and governance arrangements will be agreed upfront by COAG. During this process, COAG will determine whether and when financial incentives are appropriate and explore possible funding and distribution models.

We seek agreement of these principles by all Australian jurisdictions.

2. A NEW REFORM AGENDA

The future prosperity for all Australians depends upon a collaborative reform program with all jurisdictions achieving a nationally agreed program of change.

Nevertheless, jurisdictional responsibilities will differ.

The Commonwealth Government will play a lead role in supporting Australia's performance through maintaining stable macroeconomic conditions. The increase in the current account deficit, weak growth in non-mineral exports and shortage of skilled workers highlight the need to improve the economy's capacity and productivity. This is particularly so, if in addition to mineral exports we want to support high value-add manufacturing and services exports.

All Governments will maintain responsibility for microeconomic and social policy reforms. Here the focus will be on investments in education to increase workforce participation and productivity, improving health care arrangements, encouraging a more coordinated approach to the governance of infrastructure across jurisdictions and reducing the regulatory burden on business, and less distortionary taxation.

The combination of these reforms will facilitate a more innovative culture, securing further export opportunity and serve to raise standards of living and enhanced community welfare.

2.1 WORKFORCE SKILLS

Australia is experiencing skills shortages in key sectors of the economy, with a recent business survey finding that almost 20 percent of respondents had difficulty finding suitable labour. Governments, businesses and individuals recognise that a suitably skilled workforce is important in enhancing Australia's economic and social prosperity.

A new model for delivering Vocational Education and Training (VET) is proposed to improve the system's effectiveness and enhance its accountability. Ensuring that the

VET system is responsive to market needs is also important. Addressing skills shortages in totality, including through higher education, is necessary.

Australian Governments will collaborate to meet upcoming skills shortage challenges to bolster Australia's productive and human capital potential.

2.2 PARTICIPATION

Evidence suggests there are up to 1.5 million Australians who could potentially add to the supply of available labour. The ageing of Australia's population over the next 40 years will further limit the availability of labour supply.

Increasing workforce participation rates through policies that attract skilled migrants, promote flexible working arrangements and provide opportunities for people to either re-enter or remain longer in the workforce will become key policy priorities for governments.

While the Commonwealth Government can enhance workforce participation through its tax, social security, retirement incomes and migration policy and macroeconomic management, all governments have a responsibility to improve labour market participation rates. State and Territory Governments can have a significant impact on labour force participation by increasing educational participation and improving education outcomes. This will require additional resources.

Stronger economic growth fostered by higher labour force participation will ensure the community enjoys higher living standards.

2.3 EDUCATION

Ensuring access for all Australians to high-quality education services will enhance overall community welfare through increased social mobility and cohesion. Improvements in national education and training outcomes will boost labour force participation and create a better-educated workforce, improving productivity.

While Australia enjoys high standards of educational attainment and outcomes in general, there are worrying signs. In particular, there are greater disparities in educational achievement between social groups than in comparable OECD nations. Governments have clear responsibilities to ensure any barriers to opportunity are addressed.

The Commonwealth, State and Territory Governments share the goal of creating a lifelong high quality education and training system that leads to better outcomes for all learners, provides meaningful choices, and caters for diversity. To achieve this goal, collaboration will occur to promote consistent approaches to enhancing teacher quality, supported by improved reporting requirements to provide information on outcomes to students and parents, and drive school performance.

Improved coordination will also occur between levels of government in funding decisions concerning investment in the infrastructure and assets of educational institutions.

2.4 HEALTH

Health care costs continue to rise as a result of advances in medical technology, changing community expectations and the policy choices of governments. The ageing of Australia's population will further compound health care demands. There is scope

to improve the quality, appropriateness and cost-effectiveness of current health care arrangements. But leadership is urgently required from governments.

Collaboration by all jurisdictions in developing a shared long-term vision for health system reform is essential.

Action on reform needs to start now with clearly stated commitments on overarching goals and outcomes. Significant improvement should be expected within 3 years and major reform within 10 years.

The reform agenda must embrace the whole health and aged care system, not just jurisdictional funding issues. The aim should be to create a more 'holistic patient-oriented' health care system with prevention a key focus.

The community benefit from health care reform will be significant. The manner in which Australia supports its aged and ill provides a measure of its prosperity and national decency.

2.5 INFRASTRUCTURE

Governments need to invest in nationally significant infrastructure projects on the basis of agreed national priorities.

The first task would be for heads of government to develop an action plan to evaluate and, if appropriate implement, nation-building opportunities such as road, rail and port developments in the Melbourne-Sydney-Brisbane corridor. The task for heads of government would be to develop and implement a rolling five-year investment program in infrastructure projects of national significance.

The Commonwealth should be invited to join with the States and Territories in designing and implementing a greenhouse gas emissions trading system to apply after 2012. A major objective of the scheme would be to transmit signals to investors in long-lived assets in energy markets, mainly new electricity generation.

The Productivity Commission should be invited to review the effects of the horizontal fiscal equalization (HFE) process on investment, and consequent efficiency and productivity gained in Australian States and Territories. Recommendations should include a consideration of whether HFE should be modified or abolished. If the latter is recommended, alternatives should be provided about how adequate financial capacity through the federation could be achieved.

2.6 TAXATION ARRANGEMENTS

Progress has been made in eliminating inefficient business taxes. But reform of the personal income tax system remains an important challenge. Inefficiencies arise at both ends of the personal income tax spectrum.

To date, personal income tax reform has been an ad hoc and piecemeal process. The Commonwealth should take the opportunity presented by the current public debate to simplify and reform the personal income tax system. This would improve the pattern of incentives to work and reduce the costs of compliance. Fundamental reform is also likely to reduce levels of avoidance and evasion.

2.7 UNFINISHED BUSINESS

Victoria proposes unfinished regulatory reform from the first decade of NCP should continue. The sectors most in need of reform are energy, water, transport and communications. To improve investment certainty, further work will be required to

ensure access, regulatory and pricing regimes are appropriate and, where relevant, nationally consistent.

3. GOVERNANCE

Australians need to debate these issues. Our nation has always worked best when following a pluralist approach, where ideas and solutions compete with each other. The Victorian Government has released two papers written to stimulate this debate. No one government can or should seek to dictate what we discuss or the solutions that Australia as a community wants.

A collaborative, federalist approach for governance is envisaged, based on an equal partnership between State, Territory and Commonwealth Governments.

COAG will retain responsibility for setting the reform initiatives, determining what should be achieved and how this will be assessed, including funding and incentive options. Each jurisdiction will determine the means to achieve the reforms agreed by COAG.

Fundamental to the proposals in this Communiqué is the idea of continuous improvement in the wellbeing of Australians. Importantly, reform is not something that is just done once. It requires ongoing efforts to make Australia a more prosperous place.

Governments and citizens need to know whether reforms are achieving their aims. COAG should develop a relatively small number of measures (and associated indicators) to show whether jurisdictions are making progress towards agreed goals. These indicators would focus on the areas for reform and may include relevant measures such as productivity, workforce participation, educational achievement and skill formation, and health status.

An assessment of progress against these measures, designed to reflect the reforms agreed upon, will be undertaken for COAG by a small independent body. This organisation will have transparent working arrangements to improve upon the experience of institutions used for NCP.

PROPOSAL

Victoria calls on the Commonwealth and other State and Territory Governments to:

- (a) agree on the priority areas for reform needed to build a more prosperous Australia, including:
- a new model for delivering Vocational Education and Training, in response to market needs;
 - addressing skill shortages in total, including higher education;
 - improved labour market participation rates;
 - creating a more holistic patient-oriented health care system, embracing the whole health and aged care system, not just jurisdictional funding issues;
 - an action plan to evaluate and implement substantial nation-building infrastructure opportunities;
 - developing a rolling five-year investment program for infrastructure projects of national significance;
 - the Productivity Commission to review the effects of horizontal fiscal equalization on investment, efficiency and productivity;
 - designing and implementing a greenhouse gas emissions trading system to apply after 2012;
 - a simplified and reformed personal income tax system; and
- (b) agree to collaborate in a partnership that will determine and assess the those reforms, through:
- COAG setting the initiatives, assessment, funding and incentives;
 - COAG setting a small number of measures and associated indicators on progress to agreed goals; and
 - COAG to set up a small independent body with transparent working arrangements to assess progress against these measures.

GOVERNMENT OF VICTORIA
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