



**AUSTRALIAN CAPITAL TERRITORY**

**SUBMISSION TO THE  
COMMONWEALTH GRANTS COMMISSION'S  
DISCUSSION PAPER 2008/15-S:  
*Location – Non-wage Costs***

**March 2009**



## **Introduction**

The 2010 Review has been run as an iterative process between the Commonwealth Grants Commission (the Commission) and the States and Territories (the States) over the course of the past four years. As part of this process the ACT has provided a number of submissions in response to the Staff and Commission Discussion Papers, incorporating subsequent multilateral and bilateral discussions with Commission staff and other States. These submissions outlined the ACT's position as to the validity of the conceptual case behind a number of assessments and the proposed assessment methodologies.

It is noted that in some instances the position adopted by the Commissioners, as detailed in the latest Commission Position Papers, is at odds to that of the ACT. In the interests of brevity the ACT has not sought to reiterate the entirety of its previously stated position unless new data or new thinking has been applied. In this light, a lack of objection does not imply support where such support has not been previously stated.

## **Location non-wage costs**

The ACT is broadly supportive of the direction that the Commission is taking the Location non-wage costs assessment. The ACT acknowledges the Commission's ongoing commitment to developing this category in cooperation with the States and welcomes the opportunity to continue providing input through the location working party (LWP). Comments provided in this submission are in response to issues raised in the Staff Discussion Paper as well as issues identified subsequently through the LWP.

## **Interstate non-wages**

### **Commission's proposal**

The ACT supports the Commission's proposal to undertake further work in this area to identify appropriate cost drivers that can be used to measure interstate non-wage cost differentials. The ACT shares the Commission's concern that a piecemeal approach may overlook or omit important cost drivers and will continue working to resolve these issues through the LWP. In the interim, specific comments have been provided in response to some of the questions posed by the Commission.

### **Assessing some of the individual drivers**

Although a piecemeal approach to assessing individual non-wage cost drivers is a sub-optimal outcome relative to an all inclusive approach, where a conceptual case exists and robust data can be used to base an assessment, the ACT would support the Commission undertaking such an assessment.

### **Specific drivers – non-employee wage costs**

The Commission have proposed assessing interstate non-State employee wage costs based on the interstate employee wage cost factor. Such an assessment is premised on the belief that the drivers of State employee wage costs are similar to those of non-employee wage costs. The ACT considers this to be a reasonable assumption and believes that such treatment provides symmetry and consistency between the location wage and location non-wage assessments.

The ACT believes that strong parallels can be drawn between the State and non-State interstate wage cost assessments. In the State wage cost assessment, it has been accepted that growth in private sector wage costs are reflective of the policy neutral growth in public sector wage costs due to differential underlying labour market conditions prevalent across States. For example, if the wage costs of private teachers increase by 5 per cent, it is expected that, through competitive pressure, public sector teachers will experience a similar increase. In this way, it could be concluded that, for the purposes of this assessment, private sector employees are considered substitutes for their counterparts in the public sector.

Given this, the ACT considers that the same cost drivers are likely to impact employee costs regardless of whether they are State or non-State staff. That is to say, the same employee cost pressures are expected to impact on a State regardless of whether State employees are used to deliver a service 'in-house' or non-State employees are used to deliver it through an outsourced arrangement.

To adopt an alternative method for assessing non-State wage costs would result in an unsymmetrical treatment of what are essentially the same cost drivers, across the two interstate wage cost assessments. Such a position would also be at odds with the Commission's acceptance that private sector wage costs are reflective of those in the public sector.

### **Embedded labour costs of specific industries**

The ACT broadly supports the Commission's proposed treatment of embedded labour costs, provided in the input-output table, however, notes that there is a degree of subjectivity involved in determining each industry's pricing regime. It is thought that some broad guidelines could be used as a reality check for allocating pricing regimes between local and national. Suggested guidelines are outlined below.

Industries should be recognised as having a national wage pricing regime where:

- there is a high concentration of firms;
- labour inputs are centrally located; and
- large national firms control significant market share.

### **High concentration of firms**

Where an industry operates with oligopoly-type competition, the ACT considers it appropriate to classify its wage pricing regime as national. For example, in the mobile phone market in 2005 there were four recognisable companies competing for the market, namely, Telstra, Optus, 3G Hutchinson and Vodafone<sup>1</sup>. In situations such as these, there is a compelling case suggesting wage prices are determined nationally.

However, caution should be exercised to ensure that certain industries are not classified as national when monopolies or oligopolies operate within certain States or regions. For example, suppose there were eight companies in a particular industry but these companies did not compete nationally, instead, each provided services to one State, such as electricity generation. The geographical service areas of these companies would negate the impact of the concentration of

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<http://www.optus.com.au/portal/site/aboutoptus/menuitem.813c6f701cee5a14f0419f108c8ac7a0/?vgnextoid=72201694a15e7010VgnVCM10000029867c0aRCRD&vgnnextchannel=dcbafaf924954010VgnVCM10000029a67c0aRCRD>

firms in the market. In such circumstances, the ACT believes that a classification of local is most appropriate.

### **Labour inputs are centrally located**

Where industry participants provide services through a central office, these industries are considered to have a national wage pricing regime. An example of this may be a stockbroker located in Sydney, that provides services to State Treasury Corporations. In this instance, States can obtain services without the need for industry labour to be co-located in the State. The ACT considers Non-bank finance to be a good example of such an industry.

### **Large national firms controlling significant market share**

In some industries, although the number of firms competing for market share may be large, there may be a few firms with a majority share. An example of this is the domestic airline market. For example, in February 2009, on the Sydney to Brisbane route, Qantas offered 57 per cent of the total seats per week and Virgin Blue offered 39 per cent<sup>2</sup>. In situations such as these, the ACT considers it to be reasonable to classify these industries as having a national wage price setting regime.

### **Determining the proportion of freight sourced from each State**

The Commission has invited States to identify alternative sources of data that could be used to determine the proportion of freight sourced from each State. The ACT previously provided the data available to it in respect of freight costs to the Commission. The ACT also investigated other areas in the past to identify possible datasets that could be used to measure differences in freight costs between the States. To date, no dataset has been identified.

### **Other interstate non-wage costs**

Commission staff have indicated that they do not intend to undertake further work in this area unless States are able to provide the basis for an assessment. The ACT supports this position. There appear to be considerable policy influences impacting some of the drivers that may be difficult to exclude.

One such example is in travel expenses. There are different costs per fare to different locations. But within the cost of each fare, there are variations in fare pricing such as flexible or non-flexible, which further alter costs. In addition, policy dictates how many attendees participate in interstate forums.

### **Regional non-wage costs**

The ACT acknowledges that the regional non-wage costs element of the assessment continues to be a work in progress and notes the ability for States to provide input via the LWG.

The ACT urges the Commission to consider, as part of its analysis the:

- possibility of double counting; and
- appropriateness of applying a gradient derived from one sector to other sectors.

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<sup>2</sup> [http://www.tq.com.au/tqcorp\\_06/fms//tq\\_corporate/aviation/domestic/domestic\\_city\\_pair\\_comparison.pdf](http://www.tq.com.au/tqcorp_06/fms//tq_corporate/aviation/domestic/domestic_city_pair_comparison.pdf)

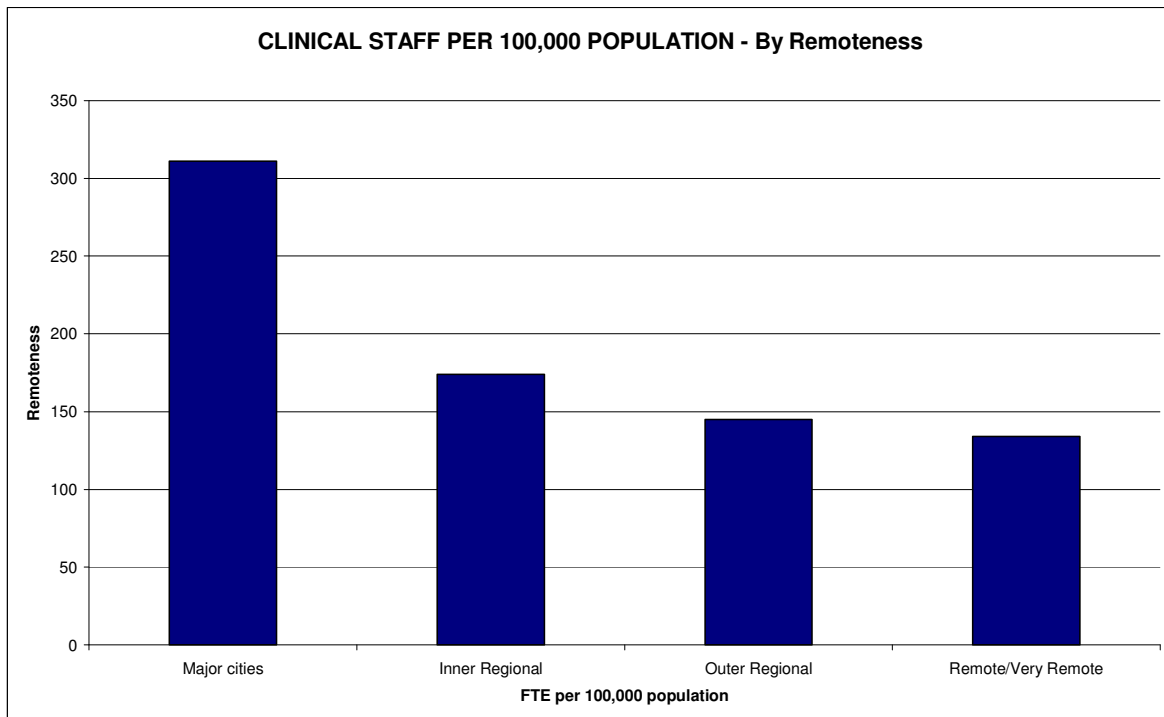
***Double counting***

The ACT is satisfied that where data can be produced that indicates the cost of a non-labour input differs between regions, such a difference in cost can be validly attributed to location effects and thus, should be assessed. However, if costs are higher in a remote location when compared to an accessible location because of differences in the quantity of non-labour inputs, these differences are considered to be driven by population characteristics – not location. The ACT is concerned that if such an assessment is included in the location category, it will be duplicating the differences in the level of service provision already being assessed through socio-demographic compositional disabilities within individual categories.

***Appropriateness of applying the police gradient to other areas of expenditure***

The ACT is concerned that the police gradient, derived from police non-wage costs per employee, may not be an appropriate measure to apply to other expenditure categories. The application of such a gradient to each State’s population assumes that there is a fixed staffing ratio per capita across all regions. For example, if there is one police officer per 100 residents in highly accessible regions, this ratio is assumed to be the same in very remote regions. This may be applicable to the police sector but staff ratios in other service delivery areas differ.

The following diagram illustrates the differences in clinical staff per 100,000 population by remoteness. Application of the police non-wage cost per employee gradient to each State’s population to measure regional health non-employee costs would overstate the expenditure in remote areas as these areas have fewer staff per capita. The ACT acknowledges that assessing non-employee location costs using the police gradient is appropriate in the police category, however, its use should be limited to the category from which it has been derived.



SOURCE: AIHW Medical Labour Force Surveys, 2005.

The ACT acknowledges that these staffing ratios may be influenced by the number of specialists located in major cities as opposed to remote regions. However, such an influence does not justify the application of the police gradient to other categories, as specific adjustments are

already being made within individual categories to recognise disabilities such as these. For example, a disability is assessed for patient transport costs in the Admitted patients assessment.

**Subsequent issues being considered through the LWP**

Due to its geographical characteristics, the ACT is unable to provide data on the extent that depreciation costs differ between regions or on staffing ratios across regions.