Rethinking our approach to regulation and governance
About this publication

The Business Council of Australia (BCA) brings together the chief executives of more than 100 of Australia’s leading companies, whose vision is for Australia to be the best place in the world in which to live, learn, work and do business.

This is a chapter of the Business Council of Australia’s Action Plan for Enduring Prosperity. The full and summary reports, and a full list of recommended actions put forward in the action plan, are available as separate publications and can be downloaded from the BCA website at www.bca.com.au.
We believe Australia’s future can be prosperous in every way, but this will depend on maintaining strong economic growth and policies that support businesses to do well.

The actions, decisions and choices we make now will either support or inhibit Australia’s prospects.

Our plan identifies nine policy areas that can deliver prosperity through well-managed growth. Across the nine areas, depicted at the end of this booklet, our plan makes a total of 93 recommendations that should be viewed as mutually interdependent actions to restore Australia’s competitiveness and lift productivity.

This booklet is focused on one of those nine areas.
Dramatically rethink our approach to regulation and strengthen governance and institutions

What do we have to get right?

We need to rethink our approach to regulation while maintaining and improving the strength and independence of Australia’s institutions and governance arrangements in order to make our markets work better.
Key facts at a glance

Throughout our history, Australia’s institutions and overall governance arrangements – including an independent judiciary, strong rule of law and entrenched system of Westminster government – have served us well. But in recent times, there has been a deterioration of good policy process and sound governance arrangements with a resulting increase in adverse unintended consequences. This is affecting our national competitiveness and resulting in growing perceptions of regulatory risk when it comes to investing in Australia.

Australia has a substantial stock of regulations – with well over half a million pages of regulation and more than 24,000 licences.

We are continuing to add to this stock at a substantial pace.

In 2011 the federal government introduced just over 7,000 pages of new legislation. Over the past decade, the federal parliament has introduced over 6,000 pages of new rules each year.

Increasing regulation is placing pressure on Australia’s competitiveness. In 2012 the World Economic Forum’s Global Competitiveness Index ranked Australia 96th out of 144 nations for regulatory burden, down 21 places from the previous year.

Significant new regulations are being introduced in Australia without being subject to due process and increasingly governments are not taking full account of the costs of new regulations being introduced.
Why do we need to rethink our approach to regulation and strengthen our institutions and governance arrangements?

Over recent decades Australia’s economic strength has been underpinned by open and competitive markets that have become more dynamic, bringing with them many new products and services and also new competitors.

A major factor influencing this outcome is the quality and strength of Australia’s regulatory system, governance and institutions.

They have played an essential role in setting and overseeing the rules that influence how the economy works and the incentives that motivate people. Sound institutions and strong governance arrangements allow markets to perform well.

Adequate property rights underpinned by efficient regulation ensure that enterprising individuals and businesses have the incentive to innovate because they allow them to have some control over the rewards that are produced from their efforts.

In practice every successful market economy is overseen by a range of institutions that regulate conduct in goods and services markets, labour markets and asset and financial markets.

Independent institutions such as the RBA and the Productivity Commission contribute to Australia’s economic performance through enhanced scrutiny, oversight and advice on our market system, both inside and outside government. As illustrated in Figure 2, these types of institutions and other governance arrangements have been built up over a series of decades.
### Figure 2: Chronology of recent regulatory, governance and institutional reforms

#### Recent history of critical regulatory, governance and institutional reforms

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<td>» Australian Prudential Regulation Authority and Australian Securities and Investments Commission established (1998)</td>
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Source: Mercer, 2012; BCA
These institutions contribute to good policy governance at a national level and help contribute to public and business trust and to confidence. They can only do so durably if they enjoy respect within government through reliable adherence to orderly process, which is central to effective influence and impact.

Having confident businesses and individuals contributing to a growing economy through investment, saving, employment and innovation in the future will be underpinned by regulatory, institutional and governance arrangements that support:

» a reasonable level of macroeconomic stability and certainty of policy settings upon which to base long-term decisions

» confidence in the government’s ability to pursue and successfully implement policy reforms that are, on evidence-based analysis, defensibly in the long-term public interest

» regulations that are clearly expressed and that are administered efficiently to protect legitimate rights

» the ability of governments to perform critical functions in the most efficient and effective manner possible, with appropriate checks and balances including impact assessments as central disciplines in decision making.

When business refers to policy predictability and stability, it is these factors that are most important. Stability is essential if we are to inject confidence into the economy. When investors put capital at risk for 5, 10 and even 20-year projects they want to know that the rules of the game are not going to change materially. Strong and robust rules and institutions are key underpinnings of any country’s competitive success.

The business community accepts that rules have a legitimate place in our society, but we are concerned about the rigour of our rule-making processes. Having well-targeted regulatory, institutional and governance arrangements can help us to compete more effectively.

Having well-targeted arrangements also reduces the risk of unintended consequences. For example, the government often introduces price restrictions with the worthy objective of protecting consumers. However, in the long term more often than not they hurt consumers by either restricting the level of investment by business or by being set at a higher level than would prevail without the restrictions.
Australia’s regulatory system may be relatively well evolved and sophisticated on some measures, but this does not mean that it is delivering efficient regulatory outcomes. Australia has well-established regulatory mechanisms such as the Regulation Impact Statement, but they are not being used to their full potential in creating an efficient regulatory system.

It will be increasingly important that the regulatory system gets the balance right in dealing with significant changes in the economy.

For example, in an economy in transition it will be important that regulation does not become a barrier to businesses being able to quickly adjust to structural pressures and for resources to flow to areas and activities where they can be put to best use. Similarly, factors like demographic and technological change will demand the most efficient policy and regulatory responses if we are to manage these changes effectively and grow the economy.

Structural adjustment will also place pressure on the role of institutions like the RBA along with increasing pressure on governments to intervene and support sectors under pressure from the high exchange rate.

Despite considerable market reforms and deregulation, Australia still has a considerable stock of regulation and it is inevitable that some regulation is impeding economic growth. Ongoing efforts to increase competition and deregulate markets have delivered considerable gains to the Australian community.

For example, National Competition Policy saw Australian governments identify about 1,800 pieces of regulation in order to review and remove as necessary restrictions that didn’t provide a net benefit to the public. As the Productivity Commission suggests, this policy contributed to Australia’s long record of unbroken growth along with strong growth in household incomes while delivering reduced prices of everyday goods like milk and electricity.
How should we rethink our approach to regulation and strengthen our institutions and governance arrangements?

A clear strength of Australia has been the high standard of our institutions and governance arrangements over many years. Having appropriately robust and flexible governance and institutions to underpin continuing economic growth will require the continual enhancement of current arrangements.

In previous chapters, this plan has focused on improvements to governance and institutions in areas such as fiscal policy, the federation and infrastructure. Therefore, this chapter focuses on how to strengthen Australia’s approach more broadly to the governance and institutions involving policy and regulation making by government and the ongoing administration of our regulatory system.

Exhibit 1: Examples of overly burdensome regulation

Environmental assessment and approvals

» The Business Council has previously cited an environmental assessment process that took more than two years, involved more than 4,000 meetings, produced a 12,000-page report and resulted in 1,500 conditions and 8,000 sub-conditions attached to approval. In total, the company invested more than $25 million in the environmental impact assessment.

Corporate governance regulation

» Even if governments implement recent proposals for directors’ liability reform, there will still be over 200 Acts with provisions making directors liable for thousands of offences.

» Current provisions under section 249D of the Corporations Act allow just 100 shareholders to require that directors convene an extraordinary general meeting. For some large Australian companies, this can involve a cost of up to $1 million on account of the wishes of less than 0.01 per cent of shareholders.

Retail restrictions

» Most states persist with highly restrictive and inconsistent trading hours restrictions. In one state alone this represents a $200 million a year cost to the economy.

Product approvals

» For medical device manufacturer Cochlear, a recent approval for an important product innovation took 14 months longer in Australia than in Europe, delaying its product getting to key export markets ahead of international competitors.
In this context, the particular policy priorities should be to:

» maintain Australia’s commitment to market-based economic principles, underpinned by the continuing strength and independence of institutions such as the RBA that are free from political interference to assess economic conditions and intervene as they see fit

» improve the performance of our policymaking processes to ensure that governments progress policy changes and new regulatory interventions in a way that, to the extent possible, they produce net benefits to the community and are in the long-term national interest

» strengthen the accountability, transparency and legislative frameworks for our regulators to ensure that they are protecting legitimate rights and supporting markets without impeding economic progress

» continually review and streamline as far as possible our existing stock of regulation

» enhance policymakers’ and regulators’ understanding of business.

Maintaining the strength and independence of our institutions

The Business Council of Australia does not see the need for wholesale changes to the well-established market institutions that have served Australia well over recent decades. It is understandable, however, that structural change in the Australian economy and pressures from global economic circumstances will bring calls from some for fundamental changes to these institutions.

As Australia approaches the 30th anniversary of the floating of the Australian dollar, there are suggestions in some quarters that currency intervention may be warranted in the face of a continued high Australian dollar, which is putting pressure on trade-exposed industries. There are also various calls and proposals for increased subsidies or increasing tariffs for trade-exposed sectors like manufacturing, tourism and agriculture.

There is no doubt that macroeconomic policy setting in Australia has become more challenging in light of structural pressures and global policy settings of zero interest rates in many advanced economies. Despite this, the Business Council does not see a strong case at this stage for the government deviating from the policy settings that have served the Australian economy well over two decades of continued growth.

In particular, the government should continue to leave the RBA to apply its independent expert judgement on the setting of interest rates (taking into account its inflation target and economic risks) and any need for direct currency intervention. It is noteworthy that the Australian dollar has eased somewhat in recent months as global economic circumstances change.

The government should also resist calls for the application of tariffs and other protections for trade-exposed sectors.

Not engaging in protection does not mean that the government should do nothing. It should instead foster the flexibility and productive capacity of the economy as outlined throughout this plan. This includes improving the skills of the labour force, removing obstacles to the movement of labour across geographic and occupational boundaries, providing temporary transitional assistance to impacted workers and companies and improving infrastructure.

The government can also run disciplined fiscal policy to reduce its impact on inflationary pressures in the economy, giving the RBA room to ease monetary policy as it sees fit.
**Policy and regulation-making processes**

There is generally a well-acknowledged sense of what constitutes best practice policy and regulation making, but with governments confronting considerable pressure to make policy quickly to deal with issues of the day, implementation in practice falls short.

Adherence to the Cabinet process by Australian governments underpins Westminster-style government. As the Cabinet Handbook suggests, it reflects the democratic principle that parliament expresses its confidence in the collective whole-of-government rather than in individual ministers.

This is underpinned by effective and timely information, as noted in the handbook:

> The principle of collective responsibility can only operate effectively if all members of the Cabinet are well informed and well advised (including by their departmental officials) about the decisions they are being asked to make. Timely and thoughtful consultation is the only way to ensure that there are no surprises and each minister has the opportunity to inform the discussion, bringing to the table his or her portfolio knowledge and political judgement. Good policy requires informed decisions.

Adherence to these processes that have served Australia well cannot be taken for granted. An increasing desire from the community for timely policy interventions and the need to handle very sensitive decisions can place pressure on the traditional Cabinet process, including the need for timely consultation.

In setting policy, governments should be increasingly cognisant that in addition to regulatory and government devices, there are a range of non-regulatory and informal devices that underpin the ethical and efficient conduct of businesses in markets.

In some instances, encouragement of these devices may be more effective and less costly than black-letter law. For example, non-regulatory devices such as the ASX Corporate Governance Council have a significant bearing on the accepted governance practices of ASX companies. Companies and their directors also have a very strong interest in upholding their reputation and professionalism, particularly given the intense scrutiny and analysis that comes from increased financial analysis and commentary in the electronic media.

Having a high-performing regulatory system means that greater regulatory restraint and rigorous policymaking processes must become business-as-usual, institutionalised through a dedicated culture among ministers and public servants.

Recognising that there are already regulatory guidance materials for governments, there would be merit in governments committing to the following principles of a high-performing regulatory system:

» Before government seeks to regulate, it must understand the problem or policy priority in depth and test the case for regulation, along with the risks and consequences of not regulating a particular activity.

» The costs of new regulation are thoroughly assessed and tested with the community through cost–benefit analysis, which includes an explicit understanding of the costs to the community including business.
» Regulation is carefully targeted to achieve its stated objectives and minimise the cost impacts on the community including business.

» Regulation is administered by regulators in the most efficient manner possible to facilitate economic progress.

» Existing regulation is constantly reviewed from first principles through new Regulation Impact Statements, with regulations amended or removed if it cannot be established that they are appropriately targeted to an ongoing risk or problem.

In addition to these general principles for our regulatory system, governments should take particular care when setting competition policies, which can have a profound impact on the effective operation of markets across the economy. There would be merit here also in adhering to some fundamental principles around competition law such as those previously outlined by the Business Council (see Exhibit 2).

**Strengthening the accountability of regulators**

It will also be necessary to ensure that regulators who administer regulation have the right incentives to balance risk with costs imposed and to ensure that they have the flexibility to discharge their responsibilities in the most cost-effective way.

This would involve establishing a more effective performance framework for assessing performance and keeping regulators accountable, including periodic reviews and dedicated independent oversight for the largest and most critical economic regulators.

Clearly the creation of a new body to oversee regulators would need to avoid the pitfalls of duplication and the creation of another layer of bureaucracy that fails to deliver improvements to government regulation. Such a body would need to have a very clear and differentiated mandate from existing bodies.

Its role would need to involve critically reviewing the performance of regulators, with the objective of driving better regulator performance and also driving streamlined regulation where poor regulator performance and unnecessary costs are the direct result of poorly designed regulation. This could have the useful benefit of better integrating oversight of the entire regulatory system – with a body that has oversight of the regulatory system at the regulator interface where the practical impact of regulation begins to materialise. An independent and empowered body would have an incentive to drive change and suggest improvements in the design of regulations and practice of regulators based on practical and objective experience.

The proposal to improve the performance and accountability of regulators in this way is not new. Almost a decade ago the Uhrig review recommended that the Commonwealth establish an Inspector-General of Regulation with a view to providing the community with a mechanism to ensure that regulators are being held accountable, and as a matter of good governance.

Investing resources in such a body is justified on the basis of the considerable cost of poorly designed and administered regulation on the community. Eliminating just a fraction of this cost each year may derive a net benefit. In addition, active oversight may ultimately reduce expenditure on regulatory bodies by helping them to operate more efficiently.
Streamlining the stock of regulation
Governments must also modernise Australia’s stock of regulation and tackle the outcomes of historic poorly disciplined regulation making.

Proper management of the stock of regulation is absolutely critical for Australia’s regulatory system to take the next step towards what the OECD refers to as ‘an embedded program of continuous improvement in regulation’.

On this basis, there are two key fronts upon which efforts to streamline the existing stock of regulation should proceed:

» embedding systematic processes and mechanisms that encourage the removal of outdated regulation and require continual evaluation and review of existing regulation, with the findings of these reviews implemented by government as a matter of priority

» undertaking targeted reviews of areas of regulation that are critical to future economic growth and meeting looming challenges.

Exhibit 2: Competition policy principles
A market-based system promotes growth and raises living standards.

For markets to work, the system must have a strong legal underpinning that inspires trust. Information must be readily available, and both individuals and businesses should be able to reap the rewards of their efforts.

Competition laws should protect the competitive process rather than particular competitors.

Competition laws should not be used to deliver broader social objectives, such as preserving domestic firms or employment.

Government businesses should not receive undue competitive advantage.

Better choices and outcomes for consumers should be the overriding goal, recognising that consumers’ interests can be met when there are many competitors or in markets with a smaller number of large and efficient firms.

Competition laws should prohibit misconduct that seriously weakens the competitive process, including predatory pricing and collusive cartel conduct.

While instances of market failure will occur from time to time and require regulatory intervention, it should be evidence-based and only introduced after broad consultation with stakeholders.

Competition regulation targeting a particular sector should only be introduced where there is clear evidence of market failure that requires it. Addressing industry-specific issues by introducing competition laws that affect the rest of the economy should be avoided.

Competition laws should be applied consistently, transparently and in a timely way to avoid creating unnecessary uncertainty.
Enhancing the performance of government

If critical government institutions, regulators and policymakers are to perform these roles effectively to underpin economic growth, then there will need to be a better level of exchange and understanding between the public and private sectors.

It will also be important to better measure the productivity of the public sector, recognising that this will not be as straightforward as it is for the private sector. The government should also institute merit-based selection processes for senior appointments to all government bodies, including regulators.

**Recommended actions**

**Action 5.1**

Australia should maintain the market approach to critical institutions that has served it so well over recent decades, including the absolute independence of the Reserve Bank of Australia, and market determination of the exchange rate. Governments should also strongly resist the introduction of tariffs and other market restrictions unless they can be shown to provide a net benefit to the Australian community. At a minimum, any new regulation should comply with the rule of law.

**Action 5.2**

The Commonwealth Government should substantially strengthen the quality and transparency of its decision-making processes. This will be achieved by:

- reinstating strict adherence to the processes set out in the Cabinet Handbook for a well-functioning Cabinet system. This includes high-quality and timely documentation along with detailed public consultation to ensure well-informed collective decision making.

**Action 5.3**

Make the preparation of Regulation Impact Statements a statutory requirement for all new regulations with a significant impact, with exemptions strictly limited to issues of national security and emergency.

- In line with the BCA’s Standards for Rule Making, the Regulation Impact Statements should have an eye to evaluation and review by establishing an evaluation plan and objective, and measurable key performance indicators.

- The recently implemented two-step Regulation Impact Statement, which requires the need for regulation to be established first before proceeding to the second step of detailed analysis, should be utilised.

- Genuine consultation should be undertaken at relevant stages of the rule-making process, with a minimum consultation period of eight weeks at each stage.

- Green paper–white paper processes should be adopted for major whole-of-economy reforms.

**Action 5.4**

Before seeking to introduce any new corporate governance regulation, governments should consult with the ASX Corporate Governance Council to assess whether the particular issue can be addressed by the council utilising its principles and recommendations.
Action 5.5

Establish a new performance and accountability code for major regulators – such as the Australian Taxation Office – which is enshrined in law. The code would be supported by provisions for:

» the establishment of an Inspector-General of Regulation to provide additional oversight of regulators, including undertaking biennial performance audits of major regulators and responding to systemic issues identified by regulated parties. Such a body could be established within the Productivity Commission with a clear mandate to take active steps to improve regulator performance and recommend the streamlining of regulation where it is impeding the efficiency of regulators and placing unnecessary costs on regulated parties.

» a balanced performance-reporting framework that assesses not only enforcement and compliance activities but the extent to which these are undertaken efficiently.

» regulators to prepare annual Statements of Accountability that outline the basis for measuring the success of the regulator, to be approved by Portfolio Ministers and the Inspector-General of Regulation.

» regulators to establish public targets on streamlining their processes to reduce regulatory burden each year.

» regulators to document, regularly update and adhere to a risk-based approach to compliance and enforcement activities.

Action 5.6

Request the National Competition Council to undertake a stocktake of National Competition Policy to build the case for further microeconomic reform. Reform should target those sectors where the National Competition Council’s original recommendations still have not been taken up and those sectors dominated by government service provision and highly restrictive regulation that would benefit from greater competition.

Action 5.7

Establish a comprehensive framework for the regular review and updating of the stock of regulation. Such a framework should include:

» implementing all of the 155 recommendations from the Productivity Commission’s annual programs of benchmarking and reviewing regulation that have been undertaken since 2007.

» extending the Productivity Commission’s ongoing annual benchmarking program by establishing rolling audits of the cumulative regulatory burden in each industry sector at least every five years, with recommendations for streamlining.

» requiring all new regulations that will have a significant increase in burden to have an equivalent offsetting red-tape reduction in the same portfolio. It may take some time for governments to establish both a meaningful and workable offsetting regime. Therefore, less sophisticated interim measures such as ‘one-in one-out’ within the same portfolio may have to be employed to even out the bias toward increasing the stock of regulation in the short term.
» institutionalising a regular refresh of significant regulations from first principles by requiring a statutory review every five years and sunsetting of significant regulations and legislation (where practicable) at least every 10 years. The terms of reference for such reviews should be set out clearly in legislation.

**Action 5.8**

In introducing National Productivity Payments from the Commonwealth to the states (see Action 1.11), priorities for state-led regulatory reform should be:

» removing duplication in environmental approvals under the Environment Protection and Biodiversity Conservation Act
» consolidating small regulators and licensing bodies
» streamlining planning and zoning requirements
» streamlining retail sector regulations, including trading hour restrictions.

**Action 5.9**

Establish a number of mechanisms to improve government’s understanding of business and incentives to reduce regulation. Mechanisms should include:

» linking ministerial remits as well as senior executive performance indicators and remuneration to the need for demonstrating efficient regulatory outcomes in their portfolios through compliance with Regulation Impact Statement requirements, as well as identifying and supporting ministers in implementing proposals to streamline existing regulatory burdens

» requiring senior executive staff to complete the Company Directors Course offered by the Australian Institute of Company Directors as a mandatory professional development activity under their performance plans

» facilitating the exchange of staff between the public and private sectors by establishing agency secondment programs, building on the secondment program adopted by the Commonwealth Treasury.

**Action 5.10**

The Commonwealth Government should charge the Department of Finance and Deregulation, Australian Bureau of Statistics and Productivity Commission with developing a framework for measuring productivity in the public sector. This could be applied as government agencies progressively adopt integrated reporting.
Prioritisation and timeline for implementation

The Business Council of Australia Action Plan for Enduring Prosperity outlines 93 recommended actions across nine policy areas that we believe will help to set Australia on the right course.

While these recommendations are intended to be actionable, it would not be possible to complete them all simultaneously. Rather, we propose that they be prioritised and implemented in three phases:

**Phase One:** those actions that should be implemented over the next one to two years, reflecting their capacity to build trust and confidence

**Phase Two:** those actions whose implementation will help consolidate our economic position over three to six years

**Phase Three:** those actions that will see the benefits of reform bear fruit and help to achieve an optimal economic performance over a six to 10-year timeframe.

Some recommendations will be easier to implement and progress than others, and some will have greater significance in terms of their potential influence on Australia’s growth prospects. As with much of public policy, a balance will need to be struck in terms of reform effort and payoff.

A suggested approach to the phasing of the recommendations contained in this booklet – and an assessment of their ease of implementation versus their overall importance – follows below.
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Action Plan for Enduring Prosperity: Rethinking Our Approach to Regulation and Governance
VISION

Enduring prosperity for all Australians

GOALS AND ASPIRATIONS

- A strong economy and full employment
- A strong society and improving standard of living
- Growing sustainably and using our resources efficiently

RESPONDING TO A CHANGING WORLD: THE CASE FOR CHANGE

- Rise of emerging economies
- Technology and digitisation
- Natural resource consumption
- Restructuring of the Australian economy
- Growth and ageing of population
Measures of success

The nine things we must get right

- Tax, fiscal policy and the federation
- Planning for population and cities
- Providing infrastructure
- Realising the potential of people and workplaces
- Rethinking our approach to regulation and governance
- Embracing global engagement
- A strong, stable and competitive financial system
- A coherent and comprehensive energy policy
- Creating the right environment and systems for innovation

Phases for policy action

- Phase One (1–3 years): Building trust and confidence
- Phase Two (3–6 years): Consolidating and growing the economy
- Phase Three (6–10 years): Realising our full economic potential and reaping the benefits

Measures of success

- A strong economy and full employment
  Australia to be ranked in the top five in the world for real GDP per capita
- A strong society and improving standard of living
  Maintain a reasonable distribution of wealth and income
- Growing sustainably
  Continue to reduce the resource intensity of our overall economic activity