INSIDE BACK COVER
I.P.A. President

21 EDITORIAL:—
M.P.s’ Pay — An Incredible Folly

24 Are We Serious About Inflation

29 Union Power —
A Countervailing Influence Needed

34 Creeping Socialism in the World of Finance
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1. To inform the Australian public of the facts of our economic system and to raise the level of economic literacy in Australia.
2. To work always for a full and friendly understanding between employers and employees and for good relations throughout industry.
3. To study the means by which private business enterprise can be made to operate better in the interests of all sections of the Australian people.

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This article went to press before the Cabinet decided to halve only the pay rises for MPs. As a high proportion of the original decision remains unaltered, this Editorial stands as a record of the Institute’s views on that decision.

Editorial —

MPs’ PAY RISES — AN INCREDIBLE FOLLY

The most formidable threat to the Government’s ability to contain inflation lies in a potential explosion of incomes. In this context, the decision to accept the recommendations of the Remuneration Tribunal for huge pay rises for MPs and senior bureaucrats is a disaster; it leaves the Government’s representations and pleading bereft of credibility. The Cabinet’s decision must be reversed. It is not too late.

As the “Review” was going to press, the Remuneration Tribunal recommended large increases in incomes for Members of Parliament and top bureaucrats. Including both salary and tax-free electoral allowances, these ranged from about 17 per cent for back-benchers and the Prime Minister, to nearly 26 per cent for the Leader of the Opposition. In between were junior Ministers at about 20 per cent and Cabinet Ministers at 23 to 24 per cent. Presumably entitlements under the notorious public service superannuation scheme will increase with salaries.

The Tribunal can, of course, only make recommendations and it is then up to the Government to accept or reject them. The Government has not always accepted all of them. This time, however, the Cabinet accepted these recommendations for very large rises, and in doing so made what might rank as about its worst decision since taking office.

It is a shocking decision for two distinct reasons. First, the public might accept, with somewhat less disgust, a rise in parliamentary and bureaucratic incomes based only on the cost of living, but certainly not one dominated by a “work value” component. Secondly, the Treasurer has for weeks been arguing the need for incomes restraint. For the Government to accept for itself such rises as those
recommended by the Tribunal is to destroy, in one supremely misguided stroke, any chance of moderating inflationary pressure by incomes restraint. The wage push is on and there can be few who do not realise it.

Of course, there will always be an outcry when parliamentarians or bureaucrats get more money. This has much to do with Australians’ extreme cynicism about the behaviour of the people they elect to represent them and also probably to the fine old Australian pastime of trying to cut down tall poppies. Whatever the reasons, it is an aphorism of politics that there is never a good time to pay an MP more. There are only bad times and exceptionally bad times. With a consummate sense of occasion the Cabinet has hit on the latter.

The Government has quite rightly pinned its hopes of economic recovery and its reputation for economic management on controlling inflation. The three principal generators of inflation are excessive public sector spending, large increases in capital inflow and incomes-related cost pressures. The first of these has proved most intractable, although the Government has worked hard at moderating its spending and at careful monetary and fiscal policies. Restrictions on capital inflow would inhibit resource development, upon which the Government has set such store. The only remaining element of inflation is wages and incomes, over which the Government has no legal powers. Instead, it has sought to exert influence by representations to the Arbitration Commission and the good example of the very moderate rise in parliamentary incomes last year. It has, in fact, achieved a good deal, in word and deed, in an industrial relations climate which can only be described as menacing to economic stability and progress. In this hazardous environment, economic management and national leadership of a high order are desperately needed.

It is on these two related grounds that the Government’s decision to accept the recommendations for raising the remuneration of MPs and top bureaucrats by around 20 per cent must be rated as a national disaster. How can this decision fail to be regarded as a green light for whatever wild claims the unions might capriciously care to make? How can a government which has been pleading, with some success, for wage restraint hope to be heeded in the future? How can union leaders, however clearly they read economic realities, put the national interest first – or indeed anywhere – in their advocacy for their members? How can the Government argue against bogus “work value” awards when 12 per cent of their rise is on just such grounds?

Often hard facts show up better in such cases than gut reaction; but even apart from the doubtful “work value” argument, this is not wholly true here. Let us first set aside the cynical argument that the right time to give MPs a small rise is just before an election, (4.5 per cent in July 1980) and the right time for a really big one is just after one (now). It is probably true that, given a high degree of competence, Federal MPs are under-paid by comparison with, say, business, the bureaucracy and State MPs; but there are at least some grounds for wondering about the standard of competence of MPs in the vital job of running the country. It may also be true that, over the last decade, MPs salaries have tended to fall somewhat behind pay in the
country at large. But it should be remembered that they have been eligible for the same scandalous superannuation scheme as the bureaucrats since 1976. It has been estimated that this would cost a private employer 30 per cent of salary on top of the normal private sector superannuation. Only an employer with a licence to print money could stand it, as T.A.A. recently found out. Thus the factual basis for the rises is not wholly solid; and, even if it were, it would still not constitute an adequate case for large, or indeed any, pay rises.

From the Institute’s viewpoint, there is an element of irony in the whole sad performance. The last edition of “Review” argued for a temporary freeze in the pay of just the people who have now, with apparent willingness, done the exact opposite. There is still an overwhelming case for reversing the Cabinet’s decision, while the fight against inflation is pursued with renewed vigour, ingenuity and singleness of purpose. Then, when the present exceptionally bad time for pay rise has subsided to merely a bad time, the questions could be reconsidered.

If this course is not adopted, the flood-gates for wild and probably irresistible wage increases will be opened with a vengeance. The Government has rightly made much of its insistence on the control of inflation as an essential prerequisite of economic recovery. It has, in large measure, staked its reputation for competent economic management on this issue. It must reverse the decision on pay rises for MPs and top bureaucrats. It simply must not fail, for the country’s sake as well as its own.

It is perhaps of value to imagine that the warnings of the Institute and others have been heeded and that the Cabinet decision to accept the Remuneration Tribunals’ recommendations has been reversed. What then? What has been lost or gained?

The first thing that must be said is that making a disastrous decision and then reversing it is not as good as getting it right first time. It indicates, not for the first time faulty judgement in Cabinet, perhaps an element of opportunism. It argues strongly for an increasingly vigilant public awareness of, and debate about, what Cabinet is doing.

The second point is that, in reversing its decision, the Government would have restored, perhaps not entirely unimpaired, its credibility in pleading for wage restraint. The power of a good example is only obvious when it is lost. By setting a good example on incomes, the Government has the opportunity to show the kind bold and forthright leadership for which the Institute has argued, and does again in the following article.
Are We Serious About Inflation?

A massive "flow on" from the Telecom breakthrough (along with the pressure on wages from the resource developments) could lift inflation toward the 14 per cent of the last year of the Whitlam administration. The threat of a wage explosion could be exacerbated by the Federal Government's questionable decision to raise the salaries of MPs and senior public servants.

All this could have serious consequences not only for the economy but eventually for the Government itself. Policies of monetary and fiscal restraint are powerless to cope with inflation, while incomes are spiralling upward. We have argued previously, and now say so again, that there is no escape from a well-rounded policy on incomes if inflation is to be substantially reduced, let alone eradicated.

We have reached a point where we should make up our minds what we are going to do about inflation. At least we should be honest with ourselves. Either we are prepared to accept inflation at around 10 per cent as tolerable – or, if not, we should act decisively to cut it back, and, ideally, eliminate it.

The former course – acceptance of 10 per cent – seems implicit in the wage-fixing principles adopted by the Conciliation and Arbitration Commission in its Decision of April 7th.* Indeed, the application of those principles could project inflation above 10 per cent over the next two years.

If, on the other hand, we are determined to stamp out inflation, then three things should by now be abundantly clear.

First, experience in this and other countries conclusively demonstrates that we cannot achieve this objective through policies of monetary and fiscal stringency. This does not mean that the monetary and fiscal weapons are unimportant in the war on inflation. On the contrary, they are very important. It simply means that they are not sufficient to win the war unaided.

Secondly, we cannot conquer inflation while we persist with wage-fixing arrangements based predominantly on prices.

Thirdly, inflation is not going to be vanquished if we adhere to "gradualist" philosophies – the concept, which has so far prevailed in government circles, of "winding down" (to use the phrase beloved by officialdom) inflation slowly. In the long run, the unpredictable inevitable crops up to throw all the careful calculations out of gear. It may be OPEC. It may be food prices. It may be something else – a steep increase in M.P.'s salaries, for instance. Moreover, the informed ones no longer take the "winding down" concept seriously – if they ever did – and base their plans for the future on the expectation that inflation will continue at a fairly rapid rate. This helps to ensure that it does.

Our opinion is that the 10 per cent rate of recent times is not tolerable and should not be accepted. The reasons are partly political, partly economic and partly to do with the community state of mind.
Let us look at the political reasons. Despite long-continued double-digit inflation in this and other countries, the performance of governments still tends to be largely judged on their success, or lack of it, in coping with inflation. (This, incidentally, indicates that most people still dislike and fear inflation). Should inflation still be running at 10 per cent or thereabouts in 1983, that would constitute a definite threat to the re-election of the Fraser administration. And should inflation in the next year or two rise significantly above 10 per cent – say to 13 per cent – that could be sufficient to tip the scales decisively against the Government.

Under present policies, a 13 per cent inflation rate is by no means beyond the bounds of possibility. Indeed, the informed view seems to be that, because of the upward pressures on wages (and therefore on other incomes) likely to stem from the resource developments, the Government could find it difficult to hold inflation at 10 per cent, let alone reduce it. From the standpoint of political self-interest, the Fraser Government, therefore, simply cannot afford to follow a “live-with-it” approach. It must, and especially because of the strengthening inflationary pressures of the moment, endeavour to find a counter-inflationary policy that will be much more effective than the monetary – fiscal disciplines it has so far pursued.

Besides the political compulsion on the Government to reject a live-with-it philosophy, there are strong economic reasons for doing so. People begin to feel insecure with anything like present inflation. With prices doubling every six to eight years, they wonder where the economy is headed. Their confidence in the future declines. Instead of concentrating their energies on productive work, many cast around increasingly for ways to protect themselves against the ravages of rising costs (including taxation) and prices. With declining confidence, the economy begins to suffer and this is aggravated by the reduced international competitiveness of a wide range of industries.

It must be said that the Commonwealth’s submission to the inquiry into wage-fixing principles (on which the Commission has chosen largely to base its decision) is hard to understand if the Government is really serious about vanquishing inflation. Indeed, the submission seems to amount to a retreat from previous attitudes when what was clearly required was a firming of those attitudes. One would have thought that the Commonwealth would have seized the opportunity to propose that the productivity or “capacity to pay” concept be re-established as the central consideration in national wage cases. Instead, it suggested that price movements – measured by the C.P.I. – be continued as the major criterion for wage adjustments. And, inexplicably, the Commonwealth went even further by proposing that adjustments be automatic, unless “exceptional and compelling circumstances” indicate otherwise. A statement by the President, Sir John Moore, on the Commission’s decision says, “In respect of wages, the Commission will treat price
movements as of prime importance”. The Commonwealth submission and the Commission's decision are tantamount to writing inflation into the economy and suggest an acceptance by the Government of a live-with-it philosophy. To this the Institute is totally opposed. The decision must mean that prices will pull wages after them, with a resulting rise in labour costs then prices and then wages all over again; and so ad infinitum. To make matters worse, the decision contemplates the possibility of additional increases for productivity improvements. Moreover, the Commission's decision states that the new principles will be given a trial for a period of not less than two years. That takes us to 1983 and election year.

It will be interesting to see how long the Government itself can live with the new set of wage-fixing principles for which it has been largely responsible. Perhaps not very long, for it has already announced its intention to launch yet another inquiry into wage fixing.

Even if the majority are “indexed” for inflation, there is a large minority which receive no such protection. The principle of indexation, besides being a guarantee of continuing inflation, is grossly unfair to fixed income receivers, many of the elderly in retirement and some welfare beneficiaries. If some sections of the community receive the benefits of indexation, there can be no good reason, in equity, for refusing those benefits to the remaining sections. Otherwise the gains achieved by some are paid for by picking the pockets of others. But the irony of universal indexation is that everyone would then achieve virtually nothing.

No one would be any better off. Indeed, in the end, every one would be worse off: because of the uncertainty and instability, the reduced international competitiveness and consequent slower growth which accompany rapid inflation.

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The curbing of demand pressures through monetary and fiscal measures, along with indexation, is clearly not going to solve the over-riding political and economic problem of inflation. Nor does the new vogue of “supply side” economics, – popular with the Reagan administration in the United States – offer a way out. Though not without good features, attempts to boost supply and productivity through tax incentives and concessions for savings and investment can, at best, operate only slowly. And “gradualism”, as experience demonstrates, does not work in the real world, however attractive and convincing it may appear on paper. Not until the Government embraces a policy aimed at slowing down the rate of growth of incomes throughout the community will its intentions regarding inflation be taken seriously. This is the nub of the matter. A well-rounded “incomes policy” is inescapable if inflation is to be substantially reduced, let alone eradicated. An “incomes policy” need not necessarily contemplate direct wage and price controls. In any case, in the Australian setting, such controls, almost certainly, could not be imposed without amendments to the Constitution.

The eventual aim of an “incomes policy” must be to brake back the growth in incomes
to accord, more or less, with increases in national productivity. This would mean the relegation of "indexation" to the scrap-heap where, on any rational assessment, it rightly belongs. Such a step would have a much better chance of general acceptance if personal income taxes were substantially cut. This would, no doubt, require compensatory increases in other taxes, a policy which, for the time being, the Government has rejected – in our view mistakenly.

A second step is for the national Government to state clearly – perhaps at Budget time – the annual increase in average incomes which can be absorbed by the economy without leading to price increases. Employers prepared to offer wage rises in excess of the "norm" thus established could be discouraged from doing so by a surtax on their profits or by the disallowance of such cost increases for tax purposes. This could be the third ingredient of an incomes policy.

A fourth ingredient is a greatly stepped-up war on tax avoidance with the threat of maximum publicity and penalties for offenders. In some ways this is at the heart of an incomes policy which would stand any chance of general support. One cannot expect P.A.Y.E. wage and salary earners to accept restraints on their incomes when they know that large numbers of people are getting rich quick through managing to avoid paying their intended share of taxes. Restraint in incomes must apply fairly and equitably over the entire community. Otherwise the policy would appear as a sham and, understandably, would be unacceptable.

Above all, restraint must apply to those responsible for administering the policy – namely, Governments, Members of Parliament and the Public Service. This is the fifth component of an "incomes policy". Indeed, more should be required, for the time being, of representatives of Government than of the rest of the community. If the former were prepared to set an example of leadership by accepting a "freeze" on their incomes for say 12 months, this could have a profound effect on the attitudes of the rest of the community. The people would know that their Government was "fair dinkum" in calling for income restraint. Needless to say, a voluntary salary "freeze" by Government, – if it were to have a convincing impact – would have to be accompanied by an overhaul of the present extravagant superannuation provisions applying to Commonwealth and State politicians and public servants. The aim should be to bring these into line with the average in private enterprise.

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The institution of measures of this kind will clearly demand intelligence and leadership qualities of a rare order. Are they too much to be hoped for? We do not think so. In the measures it has taken in response to the Lynch Committee’s recommendations the Fraser Government has shown that it does not lack political courage. It must now press on boldly. Inflation cannot be defeated without stepping on corns. But the Government would eventually earn the gratitude and respect of the community by not shirking the issue. It might even have the supreme satisfaction of demonstrating a brand of leadership unexcelled, and possibly un-
equalled in the Western World.

Three papers published recently, two from Britain, one from the United States, throw doubts on monetarism as an effective cure for inflation and suggest the need for some kind of incomes policy.

In a paper in Lloyds Bank Review, (January 1981) Lord Kaldor (Emeritus Professor of Economics in the University of Cambridge) and joint author, James Trevithick (Fellow of King’s College, Cambridge) argue that the rise in industrial prices in the post-war period was, in the main, cost-induced. “It had virtually nothing to do with excess demand”. They conclude, “How is this inexorable upward pressure on money wages — a pressure which is independent of aggregate demand — to be contained? The most feasible solution . . . is to devise a national policy on the determination of money wages”.

The Midland Bank in its 1980 Winter number, proposes that consideration be given to supplementing monetary and fiscal restraint with an incomes policy in order to preserve the level of employment and output. With incomes rising more slowly, employers would be more inclined to engage more workers and this would help to offset the contractionary effects of a tight monetary policy.

Finally, in a comprehensive examination of inflation in the United States (published in “The Economist” of March 21st) the author, Francis Bator, Professor of Political Economy at Harvard University, concludes, . . . vanquishing inflation has to remain a primary goal. It is not a goal we can achieve merely by compressing demand and trying to boost productivity. However, distasteful to business and labour (and to most economists) we must supplement fiscal, monetary and supply-side policies with a flexible but mandatory incomes policy. There is no tolerable alternative.”

That, broadly, is also our conclusion.

* THE NEW PRINCIPLES OF WAGE FIXATION

1. Other than in exceptional and compelling circumstances wages will be automatically adjusted by 80 per cent of the C.P.I. movement for the December and March quarters.
2. The Commission will give consideration to adding the remaining 20 per cent of the C.P.I. movement plus the movement in the June and September quarters at a final Review later in the year.
3. Productivity adjustments will also be considered at this hearing.
4. The principles will apply for a period of not less than two years barring compelling circumstances.
Union Power – A Countervailing Influence Needed

It is not new to regard unions as too powerful for the country’s good; nor is this view restricted to employers. The remedies put forward over the years have generally called for governmental action, and have generally come to naught. While there are no panaceas, there might be scope for action by employers in their own interests – and in Australia’s.

Not so very long ago, bosses gave the orders and employees obeyed them. Working conditions remained generally poor long after the industrial revolution gained momentum. Discipline was severe and job security virtually non-existent. Then, as the union movement painfully grew, employers gradually found that their authority was increasingly challenged, the balance of power was swinging – or being propelled – away from them and towards the employees, or perhaps more accurately, towards their union leaders. To the rise of the trade union movement must be attributed this massive swing in industrial power. As an old-style Labor man, – and an eminent Australian – put it “the unions are now doing to the bosses what the bosses once did to the workers”.

The pendulum of industrial power has indeed swung from one extreme to the other. Yet few, even among more backward-looking employers, would wish to see the disappearance of the union movement. This should not be taken to suggest that, industrially, everything in the garden is lovely. On the contrary, there has been for many years a widely held belief that the unions are too strong, not only for the convenience of the bosses and the wealthy, but also for good of ordinary working men and women and for the nation as a whole.

The most conspicuous, but possibly not the most important, manifestation of union power is in bargaining on wages and conditions for their membership. Employers, especially in the private sector, almost invariably give the impression that they are fighting a rearguard action against overwhelming odds. They know they are unlikely to win. The only question is how badly they will lose. In such one-sided negotiations there appear to be only two stabilising influences. There is the clanking arbitration machinery, going through the motions of applying a veneer of respectability to unbridled union power in the interests of industrial “peace”. Much more importantly, the intuitive wisdom of rank-and-file union membership is possibly the only economic sheet-anchor we possess in the face of powerful and often militant union leaders. Such leadership must be expected. There is an element of the illogical in the often-heard call for union leaders to act “responsibly”, if it means their getting less than they could for their members.

Another consequence of union power passes practically unreported. Yet it may well be more damaging to this country than union-forced wage rises. This is the inhibiting effect union power has, by its very existence
and without overt effort, on investment, technical innovation and productivity throughout industry. Of course, senior management would be directly involved in decisions on major capital investment and would be well aware, for instance, of new pay rates and manning schedules for new plant. However, in other areas involving junior to middle management, such as work methods, layout of plant in manufacturing and technical innovation not requiring significant capital, the effects of union power are more subtle and therefore much less obvious. Improvement in these areas, however clear the possibilities may be, will probably never see the light of day if they would stir up any significant industrial problems. For the management directly concerned with these improvements, rewards for success are likely to be slight and the penalties for failure severe.

A third, entirely understandable consequence of the power of unions is its levelling effect on the work performance of their members. In a system placing emphasis on solidarity and the "rate for the job", levelling inevitably means levelling down, since not all can match the performance of the best. While it is not easy to assess the influence of this levelling on performance and job satisfaction for the individual, or on the productivity of industry as a whole, its effect can scarcely be negligible and may be formidable.

It was earlier remarked that, often for good reasons, there is remarkably little discussion of the more subtle effects of union power. Coincidentally, a recent survey (Perspectives in Productivity, conducted by McNair Anderson on behalf of Sentry Holdings Ltd.) throws unusually interesting light on these effects. Five classes of people were asked "which group or groups (of nineteen) . . . are mainly responsible for this country's productivity not being better than it is?" It is not altogether surprising that 94 per cent of executives in secondary and tertiary industry considered that trade unions were mainly responsible, or even that 82 per cent of public servants canvassed also thought so. What is highly remarkable was that 73 per cent of the work force gave the same answer.

There is nothing very novel in the economically damaging phenomenon of overwhelming union power, to which this survey is eloquent testimony. Industrial problems dominated the first editions of the "Review" in 1947 (which was published by what was then significantly called the Industrial Committee of the I.P.A.), one of which said "The Trade Union movement wields tremendous power over the economic and industrial future of Australia" and asked "Will it use this power wisely?" It is unlikely that the victims of this winter's power shortages will be in doubt about the answer to that. Yet the Institute's view of the labour relations climate, all those years ago, was not so very different from today's: "The industrial situation in Australia has rarely been more serious in its political implications, or more destructive of material, social and moral standards than it is today. . . we have slipped so far down the abyss of industrial hostility and conflict that many look askance and rather hopelessly at the long and difficult climb back". This has a
discontent, and about it, in view of the experience during the long intervening years.

Even more forlorn sounds the Institute's 1947 opening to a discussion of possible solutions to the exercise of union power: "The best time to deal with disrupters is now, not when they have grown in strength and authority". Today, solutions are no nearer. Over the years, some have come to be regarded as "not on"—e.g. strike breaking by volunteer labour or the armed forces. Others have been swamped by the tide of socialisation—e.g. "over-high taxation (that is, by 1947 standards!) can be a powerful cause of frustration and dissension in the industrial sphere". It can always be argued that other remedies have been insufficiently pursued. Perhaps governments over the years should have preached harder about the need for better employer-employee relations. Secret and compulsory ballots for the election of union officials and for strike votes have been much discussed over the years but never made mandatory. The so-called "penal clauses" in arbitration legislation have themselves been a victim of the union power they sought to control. Thus, doubtless for superficially persuasive reasons, none of the principal suggestions for the moderation of union power has been put into effect over the post war years.

From this sorry tale several conclusions may be drawn. First, the economically damaging and often extreme exercise of union power will not go away of its own accord. It will get worse. Secondly, governments are practically powerless in the face of unions. Those who clamour that "they" should do something, or who would like extreme measures against unions, are unrealistic. Those who come forward with moderate and practical proposals for official action tend scarcely even to appear to be given a hearing. Thus it is, nowadays, evidently unreasonable to expect any effective action from governments to redress significantly the huge imbalance of power between unions on the one hand and employers—indeed the nation as a whole—on the other.

It is the third conclusion which may well introduce more than just a spark of hope into a tale otherwise desperately devoid of it. There are two broad approaches to the lessening of this imbalance of power. The one almost universally espoused, and already discussed, is for one form or another of restrictive action by government to reduce the power of unions. It has been suggested that to expect effective action from this source is to bay for the moon. The other broad approach is to increase the power of employers to resist union action. It must thus be concluded that the economic well-being, stability and dynamic of this country may yet depend on the capability of employers for concerted action.

This will not be easy. It will probably not be cheap. It may well involve something of a mental revolution in employer thinking. The essential but mortifying achievement of unionism is the enforcement of unity by the stamping out of ambition and competition among their members. By contrast, employers start with the great psychological disadvantage of being competition-oriented (This remains generally true even when the corporate environment has elements of monopoly
or cartelisation). Of course, competition is the very essence of the enormously productive free enterprise system. But competition among employers for the purchase of labour, the supply of which is monopolised by a union, places them at what in practice amounts to a fatal disadvantage. On top of this, taxation and other forms of governmental pressure on free enterprise have risen enormously over the years. These factors have combined to limit greatly the ability of companies to withstand interruptions to normal working and hence to act in concert to resist union muscle.

This suggests that an effective countervailing influence, enabling employers to act with greater unity, might be the availability of financial support in the event of industrial action. An obvious means of providing this kind of support would be by normal insurance. This has problems where the actions of those insured could materially alter the risk and hence the potential payouts, a situation known in underwriting jargon as "moral hazard". Another possibility is a mutual fund, the members of which in effect agree to insure themselves against a common risk. All schemes, at present either operating or under consideration around the world, appear to be based on the mutual fund concept. This is true of the scheme under consideration by the Confederation of British Industry, which is experiencing a prolonged gestation period. It is designed to give members cover against losses arising from standing charges during strikes, but not loss of profits. The concept is for a wide coverage of British industry, a characteristic it shares with West German and Swedish schemes. The latter has been gaining strength steadily, and last year apparently weathered well Sweden's largest labour dispute, a ten day strike/lockout amounting to a general strike. In a year of considerable industrial unrest, the fund only had to pay out about 12% of its accumulated funds in compensation during 1980.

Elsewhere, schemes are on a more restricted, typically industry, basis. In the U.S.A. there are such funds for air transport, newspapers, railways and sections of agriculture, all now long established. In Britain, there are "clubs" on the same basis to protect shipowners from losses occasioned by port stoppages. Thus the schemes already operating differ greatly in scale and in the industries they cover. Possibly, too, there is no exact parallel of union structure and arbitration machinery between Australia and countries where schemes are working successfully.

In spite of these considerations, it is hard to see why a scheme, on the lines of those overseas, could not be tailored to suit the needs of interested companies here. Of course, premiums would have to be based on tiers of relevant risk criteria; while payouts would aim to give the best possible support to members, given that the fund should be so designed as to be unbreakable (by, for instance, concerned union action to that end) and to grow as quickly as possible in its early years. As the scheme became stronger, an element of re-insurance might be possible, as also might be the reduction of premiums.

As such schemes as these are relatively novel in Australia, if not overseas, it is
worth considering briefly some of the objections which might be raised. Of these, perhaps the most obvious is cost, which would probably vary widely from one industry to another and even among companies. As against this, it has been suggested that the benefits would not stop at the inhibiting effect on the propensity to strike. A reasonable expectation might be an improvement in this country’s fairly lamentable rate of productivity improvement, rendered possible by a degree of loosening in the restrictive and conservative influence of unions in industry.

Another possible objection is that unions might launch a “pre-emptive strike” against participants in such a scheme, to try to break it in its infancy. The success of the scheme would then depend on how well it was constructed and on how badly employers wanted to do something positive to improve this country’s industrial relations climate. In Britain at the moment, a group of Lloyds brokers are offering a strike policy which has run into opposition from unions, who claim that it would enable a company to wait out any strike. While this is a gross exaggeration, it does suggest that the unions regard even this restricted scheme as potentially effective in limiting their power.

A third possible objection is that a scheme of this sort would never be likely to give employers dominance over unions, however strong and well established it might become. This objection must be sustained. It is hard to see the mutual fund approach ever becoming strong enough to deprive unions of their ability to look after their members.

It is not the Institute’s intention to claim a panacea for industrial problems, still less to make proposals which might lead to a swing of the pendulum completely in favour of employers. Rather, the object is to work towards bringing the pendulum of industrial power to rest in the centre; to provide, in short, a countervailing influence to the present overwhelming power of the unions. The attractions for employers are obvious. They could negotiate with unions, either through arbitration or across the bargaining table, on a basis of something better than complete underdogs and perhaps, in time, as equals. Perhaps it would not, then, be too much to expect gradual and a general thaw in this country’s industrial relations climate. The implications of this for productivity improvement, for the size of the national cake are and for the dynamism and vitality in industry are enormous. So, too, are the potential benefits for this country.
Creeping Socialism in the World of Finance

The article discusses the means by which Government owned insurance offices have expanded, in recent years, at the expense of the private insurance offices. It also details the costs of this expansion, not only to the insurance industry, but to the private sector as a whole. Some suggestions are advanced as to how governments might change the ways in which they handle their insurance offices, for the benefit of the Australian economy.

There has been much debate in recent months about the need for Government to withdraw from functions more appropriately handled by private enterprise. Indeed the Federal Government took a step in the right direction when it accepted the recommendations of the “Lynch Committee”. However, relatively little attention appears to have been given to government participation in the financial sector through its ownership of banks, life and general insurance offices, permanent building societies and finance companies.

The Commonwealth is represented in the financial sector by such “trading” arms as the Commonwealth Trading Bank and the Commonwealth Savings Bank (which has an internally run housing insurance scheme) the Australian Industry Development Corporation; the Defence Service Homes Insurance Scheme; the Housing Loans Insurance Corporation; Medibank and The Export Finance and Insurance Corporation.

Each State and the Northern Territory has its own government insurance office. Each State, except Queensland, has its own State Bank; South Australia has two such Banks. The Queensland Government Insurance Office has strong links with a permanent building society while the New South Wales Government has a building society of its own.

The Federal Government has taken a first step towards reducing involvement in the financial sector by announcing its intention to sell the Housing Loans Insurance Corporation to private enterprise. However, if various recommendations of senior public servants and politicians – socialist and non-socialist – are accepted we can expect expansion of public trading activity by the State-run institutions. Thus, incredibly, a Federal Liberal M.P. wrote a letter to a national newspaper in 1979 arguing that Queensland should not be denied the advantage of having its own State Bank.

Another example of the pressure for greater government participation in the financial sector, coming from a quarter that might have been expected to support the private sector, occurred prior to the 1979 State Elections in Victoria when the life insurance industry sought the attitudes of the various political parties about the role of the State Insurance Office. While the reply from the then Premier (Mr. Hamer) was not unexpected – “The government has not at any time contemplated the entry of the State Insurance Office into this field, and it has no intention of changing its policy” – the response from the leader of the National Party was a little surprising. He said: “In relation to the State Insurance Office, I would point out that my party
believes it is quite illogical that the State Insurance Office should have to act in the way it does at the present time. It should either be wound up or allowed to compete in all fields of general insurance. For political reasons it would be very difficult to wind it up as there are so many people presently employed in the State Insurance Office”.

Pressure for greater government participation in the financial markets also comes from the government owned offices themselves. Thus, the Insurance Commissioner in Victoria, who also serves as the chief executive officer of the State Insurance Office, is not content with the immense advantage of a government-backed guarantee. He has called periodically for the right of the State Insurance office to transact all classes of business, which would ultimately include life insurance. The franchise of the office is at present limited to the writing of compulsory third party insurance, a market of which it has a monopoly, other motor insurance, in which field it has one of the largest market shares in the State, and workers’ compensation insurance, where it has the largest market share.

The executives of Government financial enterprises, not only work to extend their own area of activity, but they also encourage the development of similar institutions in other places. Thus, a former Commonwealth Life Insurance Commissioner—who is also a board member of the Tasmanian Government Insurance Office—was involved in the establishment of the Northern Territory Insurance Office, and now serves on the board of the Territory Insurance Office.

Once established the various government financial corporations tend to reinforce each other. For example, the T.I.O. (The N.T. Insurance Office) has an agreement with Medibank Private, which permits the T.I.O. to receive membership contributions and, more importantly, operate claims cash centres through the branches of the T.I.O.

This article concentrates on Government participation in general insurance and leaves aside the important areas of banking, permanent building societies, finance companies and life and health insurance.

20.3 PER CENT TO 36.7

In 1970-71 the public sector had 20.3 per cent of Australia’s general insurance market. By 1979-80 the government share was 36.7 per cent—38.7 per cent if we omit reinsurance, an area in which government insurance offices do not yet compete.

The objections to government participation in the general insurance field are twofold. First, government sponsored offices do not compete on an equal footing with the private offices and, secondly, government offices do not always act in a way which is consistent with the most effective operation of the economy and the best interest of the community.

Of all the advantages held by State Insurance Offices the greatest is their government guarantee. In an industry such as insurance, where security is paramount, the guarantee is unsurpassed as a tactical weapon and gives government offices a huge marketing superiority.

Advertisements in which government insurance offices capitalise on this advantage to undermine the business of the private
sector are not uncommon. A State Insurance Office advertisement in Victoria concluded with "State Insurance is the only insurer guaranteed by the Government of Victoria. State Insurance as safe as the State you live in". The State Government Insurance Commission of South Australia published an advertisement consisting of a montage of headlines from newspapers proclaiming insurance company collapses, critical problems for the insurance industry and private insurance facing extinction. In bold type appeared the words "FORTUNATELY FOR YOU, WE NEVER MAKE THESE HEADLINES". Then followed the message: "If you end up going down with your insurance company, you're better off not being insured at all. But with S.G.I.C. you're safe and secure . . ."

It is ironic that many of the taxpayers providing these guarantees are still insured in the private sector. However, if they wish to obtain the benefit of "their guarantee" they must abandon private enterprise and move their policies to government insurance offices. And yet the same "guarantors", are helping through taxes to pay some of the over-generous superannuation benefits provided for public servants employed in public trading bodies. It seems that these organisations will not be able fully to fund their superannuation schemes out of their own resources and, like T.A.A., will require assistance of taxpayers - "clients" or not.

Among the most outrageous and intolerable features of the operations of government insurance offices is the use of policemen as paid part time agents in country districts in Queensland and Western Australia. In many country areas in Queensland, clerks of court, other than police officers, are also paid agents. There is obvious potential for conflicts of interest in both situations.

Government insurance offices have the advantage of obtaining support services from other government bodies. Thus in the case of the N.S.W. G.I.O., the "Interim Report of the Select Committee on Public Accounts and Financial Accounts of Statutory Authorities (1978)" states:--

"Among the Government departments known to provide services for the G.I.O. are:--

(a) The State Electoral Office - whose computer file was used by the G.I.O. to enable it to follow up lost clients, and also for claims purposes. (The N.S.W. Privacy Committee recently reported adversely on this practice).

(b) At a Royal Commission in Western Australia in 1974, the G.I.O. of N.S.W. acknowledged it made use of some Clerks of Court in country N.S.W. as agents.

(c) The G.I.O. has used, and presumably still uses, Government printing services and the G.I.O.'s staff were, and are no doubt still, paid via the Government's central computer system in the Treasury.

(d) In the 1976 Annual Report of the G.I.O. it was acknowledged that the office was "indebted to the Public Service Board, Department of Motor Transport and other areas of Government for services rendered".

Even if the G.I.O. pays for these services, it will almost certainly be paying less than
market price, since the bodies providing the services are not operating on the basis of normal commercial criteria. Thus, taxpayers in N.S.W. are subsidising those who choose to do their business with a government owned office.

**EXEMPTION FROM TAXES**

The payment of taxes is another area in which the government insurance offices have advantages over private companies. Government owned enterprises are generally exempt from Federal and State taxes. Usually, however, State insurance offices make arrangements to pay their State Governments an amount equal to the tax which they would have had to pay had they been private insurance companies. But taxes or their equivalents are not always paid. In 1978, it was noted in a N.S.W. Parliamentary Committee report that the N.S.W. Government Insurance Office “has escaped paying over $1 million” in stamp duty.

The Government operated Worker’s Compensation Board of Queensland, which has a monopoly of workers compensation business in the state, does not pay any income tax. Similarly the Commonwealth Government’s Defence Services Home Insurance Scheme, one of the largest home insurers in the country with some 200,000 dwellings on its books, appears to pay no income tax, sales tax or payroll tax.

Another example of “tax avoidance” by government insurance companies can be found in the 1980 annual report of the Territory Insurance Office:

“The Minister may, by notice in writing to the Board, require the office to pay to the Consolidated Fund of the Territory such amount as he considers would have been the liability of the Office to pay income tax under the Income Tax Assessment Act, 1936 of the Commonwealth. No such notice has been received in respect of the year ended 30th June, 1980 and therefore no amount has been provided for payment to the Consolidated Fund”.

The major advantage available to the Government insurance offices is the ability to acquire for themselves by what can only be described as unfair government tactics, a substantial portion of the insurance market.

**THIRD PARTY INSURANCE MONOPOLY**

The major factor contributing to the growth of premiums and assets in public sector insurance is the large volume of compulsory third party insurance premiums received by State Government insurance offices and similar bodies. They have monopolies of this business in South Australia, Tasmania, Victoria and the Northern Territory and the lions share of the premiums elsewhere. For example, the Government Insurance Office in New South Wales has probably about 98 per cent of the market in that State, while the State Insurance Office in Victoria is the only one handling compulsory third party insurance. Private insurers have been driven from the field partly because of government control of premium levels. Often actuarial and Premiums Committee recommendations have been ignored in favour of political decisions to keep premiums below the true cost of cover. One could argue that in the absence of political interference, premiums would at times have risen to a level which would have caused a public outcry, leading to an attack on the root cause of the problem.
road accidents and deaths. One might then conclude that many lives in Australia could have been saved had remedial action been taken earlier by governments – promoted by a vocal public confronted by the real and visible cost of road injuries and deaths.

Apart from premium constraints, with charges usually fixed by the government at an uneconomic level, virtually limiting the field to offices which have the benefit of a government guarantee, the Federal Insurance Act requirements prevail. In Victoria, RACV Insurance which had a large share of the compulsory third party insurance market, was the last private insurer in the field. However, it was forced to withdraw in December 1976, despite its wish and that of the Victorian government for it to remain. Six-month long negotiations involving the Victorian government, the Federal Insurance Commissioner’s office and the RACV came to naught, foundering on the fact that RACV Insurance could not meet the Insurance Act’s solvency requirements. The solvency requirements of the Federal Insurance Act 1973, allows insurance companies a premium income of up to six and two-thirds times its shareholder funds. However, compulsory third party insurance is considered by some State Government insurance offices to warrant special treatment for Federal Insurance Act purposes. Although the government offices escape the Act’s application, they sometimes convey the impression that they comply with its general provisions. For example, Victoria’s State Insurance Office has stated it complies with the solvency ratios “in any area where private sector insurers are competing” but added “this excludes compulsory third party insurance business”.

The public sector, with a stranglehold on compulsory third party business, has access to vast and rapidly-growing amounts of outstanding claims reserves from compulsory third party insurance.

In 1979-80 the total assets of government insurance bodies eclipsed for the first time, the assets of private insurance offices (excluding reinsurance) – $4,342 million to $4,135 million. (In both cases the figures exclude Life Insurance Statutory Fund Assets). While public sector bodies made a collective underwriting loss of $48.5 million, direct underwriters in the private sector produced losses of $150.7 million. However, particularly significant is the performance of either sector after investment income is taken into account. For the public sector a total of net profit before taxation of $234.0 million resulted, compared with $165.1 million for private enterprise direct insurers. The respective provisions for taxation were $35.2 million and $51.5 million resulting in total net profits of $198.8 million for government insurance and $113.6 million for private insurers. The relative performance of the two sectors in 1979-80 are not unique and follow the general pattern in recent years.

THE TERRITORY INSURANCE OFFICE

The Northern Territory’s government insurance office was recently created by a Country Liberal Party Government. The Territory Insurance Office opened for business in July 1979 and its first annual report has now been issued. The modus operandi

IPA Review — April-June, 1981
of the T.I.O. is not dissimilar from what private-enterprise insurers have learned to expect from government insurance bodies—both Commonwealth and State.

The nucleus of the office’s business is a monopoly of all compulsory third party insurances. Expenses have been arbitrarily apportioned over the various classes of business, leaving the monopoly class of business heavily subsidising the expense of those policies sold in competition with private insurers. In fact, it appears that the expenses for the latter policies have been overstated by at least 100 per cent—which, in effect, leaves motorists unknowingly subsidising the government office’s operations and perhaps allowing it eventually to drive private companies out of business.

**WORKERS COMPENSATION INSURANCE**

Workers’ compensation insurance is another valuable source of funds for State governments, particularly in Queensland, where a government Board writes the business as a monopoly class, and in New South Wales, Victoria, South Australia, Tasmania and Western Australia, where the government insurers are either the largest or near-largest underwriters of the business. Workers’ compensation insurance for all coal mines in New South Wales and all mining activities in Western Australia is a monopoly of government insurance.

Within the last two years, the Government of New South Wales directed to its Government Insurance Office workers’ compensation public liability and other insurances on public hospitals. The total amount involved exceeded $20 million. Government business directed to government insurance offices amounts to scores of millions of dollars each year, affecting materially the whole cost structure of government insurance offices. It brings them the benefits of economy of scale; it depresses their expense rates markedly; it gives them the opportunity to charge premiums the private sector finds difficult to match. It is sobering to reflect that there would be a monopoly airline in Australia today had the Federal Government not provided in the Airlines Agreements Act that the private carrier must receive 50 per cent of all mail carried by air.

**INVESTMENT OF FUNDS**

Government participation in the insurance business is at a cost not only to private insurance companies and their policy-holders but to all business in the private sector. With similar funds to invest, the pattern of investment by government companies is quite different from that of private sector insurance companies. Almost half (45 per cent) of the assets of the public sector general insurers are in the form of government or semi-government securities. Only 20 percent of their assets are in the form of equity investment or loans to private companies (other than mortgage loans). The private insurers on the other hand hold only 11 per cent of their assets in the form of government and semi-government securities; while over one-half (57 per cent) are held as equity investment in or loans to private industry (other than mortgage loans).

Government participation in the general insurance field has thus cost private industry hundreds of millions of dollars of investment funds. To make things worse there have been occasions when State Governments
have instructed their insurance companies
to direct their funds to specific areas of
activity or enterprises on the basis of political
expediency rather than economic merit.
Sometimes this has been done deliberately
to frustrate the legitimate investment plans
of private enterprise firms. An example of
this type of interference occurred in August
last year, when the South Australian
(Liberal) Government introduced legislation
to enable the State Government Insurance
Commission to purchase certain shares in
the South Australian Gas Company. The
purchase of the shares was to give the South
Australian Government control of the South
Australian Gas Company and prevent a
takeover of the company by a firm from
another State.
The Queensland Government has used
the State Government Insurance Office on
a number of occasions to prevent the takeover
of public companies based in Queensland.
Of the 52 public companies based in
Queensland in 1979 the S.G.I.O. appeared
among the top 20 shareholders in 21 cases—
in several cases following an attempted
takeover by a non-Queensland company.

**TOWARDS FAIR COMPETITION**

It may be true, as the Leader of the
Country Party in Victoria suggests, that
State Governments cannot easily divest
themselves of their insurance companies—
at least not in the immediate future. Never-
theless there are a number of things govern-
ments can do to alleviate some of the
damage stemming from the way in which
they are participating in the general insurance
market at present. Above all, State Govern-
ments must resist pressures to allow state
insurance offices to extend their activities
into new areas. This would, at least, prevent
state insurance offices from taking an even
larger slice of the insurance business for
themselves than they have managed hitherto.

Next, steps should be taken to remove
the advantages that government companies
have over their private sector counterparts.
This should be done in three ways. First,
market forces should be allowed to play a
greater role in determining compulsory third
party insurance premiums. This would allow
for greater private sector participation in
this area of insurance. Secondly, Govern-
ment must not compel or even encourage,
government or semi-government organisa-
tions to insure with government-owned in-
surance companies. All those seeking
insurance should chose between suppliers
competing (on equal terms) in the market
place. Thirdly, governments must make
sure that where their insurance companies
obtain the services of other government
departments or agencies, they are charged
the market price equivalent of the service.
At present some Government insurance
offices obtain services from other govern-
ment bodies at less than market price. Such
a price embodies a subsidy from taxpayers
to the state insurance offices and their
customers.

Finally, governments must allow their
insurance offices to invest their funds more
in accordance with normal business criteria.
At present almost half the funds of the state
insurance offices are on loan to government
or semi-government bodies. If they were
allowed freedom of choice, we could expect
government insurance offices to divert
hundreds of millions of dollars away from
the public sector to more profitable private
sector business.
I.P.A. PRESIDENT

Sir Wilfred Brookes, C.B.E. D.S.O. A.E.A., who has served as President of the Institute of Public Affairs since 1972, retired on the 30th June. Sir Wilfred's devotion to the affairs of the Institute over so many years is widely appreciated in the business community as well as by his colleagues on the Council and the staff of the I.P.A. He will, we are pleased to say, remain a member of the Council, where his experience will be invaluable.

Sir Wilfred is succeeded by Mr. J. S. Balderstone, who is well known in business and pastoral circles in this country. He is a director of the Commercial Bank of Australia, the Broken Hill Proprietary Company, the A.M.P. Society and Woodside Petroleum, and recently retired as Managing Director of the Stanbroke Pastoral Company Pty. Ltd.

Mr. Balderstone will be only the fourth President of the I.P.A. since it was established nearly forty years ago. Preceding Sir Wilfred Brookes, were Sir George Coles, C.B.E., and Mr. Eric Lampe, C.B.E. both of whom, as members of the original Council, were among the founders of the I.P.A.