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Working Together: Towards an Inclusive Federalism?

Campbell Sharman

I was probably asked about the title of my paper, and may well have agreed to the present one, but it looks now like a mild contradiction in terms (the question mark is my subsequent addition). It reminds me of Tony Blair's comment in his address to the recent British Labour Party Conference that he was committed to 'compassion with a hard edge'. This is not in the same class as those great oxymorons like a 'deafening silence' or 'military intelligence', but it has a certain appeal. 'Working Together: Towards an Inclusive Federalism?' could be in the same category. The whole point of federalism is to have several governments that distrust each other in a way that produces enough tension and competition to make the system work properly (see Dye, 1990:ch. 1). Federalism is about the constructive use of distrust, not about working together in harmony. Governments that work together inclusively are the worst kind: they are (with apologies to Adam Smith) almost certainly planning some conspiracy against the public or some contrivance to raise taxes.

The idea of designing a system of government in which ambition fights ambition is a very old one (Ostrom, 1987). It underpins the idea of constitutionalism on which our system of liberal democracy is based. The separation of powers between the legislature, the executive and the judiciary is designed to disperse power between various agencies of government so that they can act as a check on each other and prevent the concentration of power that leads to the arbitrary and dictatorial use of government authority. Only by setting up institutions that are designed to oppose each other can openness, accountability and responsiveness to the public be guaranteed.

Federalism takes this process an additional step by dividing power between a central government and State governments that represent regional communities. In this way, the States can represent the interests of their political communities and carry out policies that reflect the preferences of regional majorities whether or not these policies would be supported by a national majority. Central governments are responsible only for those matters where, as the economists would say, externalities

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abound: that is, only those matters which necessarily affect the interests of residents across the federation and cannot be dealt with through joint action by State governments (Ostrom, 1974).

Such a system of government has many advantages. It not only provides a governmental structure that reflects regional preferences more efficiently than a unitary government, but it sets up constitutionally entrenched governmental units that can monitor the activities of other governments. There is no more effective way of checking the action of one government than by the counter-action of another government. Given the ineffectiveness of some of our parliamentary institutions, public dispute between the various spheres of government may sometimes be the only way in which the openness and accountability of government actions can be ensured.

If federalism is such a wonderful system of government, why are there frequent complaints about it and repeated suggestions to alter the way it operates? Is there something wrong with the design of the Australian federal system? I would be the first to concede that the answer to these questions depends very much on one's point of view. Much of the problem with debates over the Australian federal system, at least until recently, was that they were like the sound of one hand clapping: there was a great deal of criticism but little support (Galligan, 1995:ch. 2; Sharman, 1992). There has been a long tradition of complaints about federalism precisely because it divides power and checks governments. This attitude is derived from the same majoritarian tradition that criticises the Senate, constitutional referendums, and judicial review of the Commonwealth Constitution because these institutions prevent the government of the day being able to do exactly what it likes in the name of a popular mandate. This view has long characterised the attitude to federalism held by the Australian Labor Party, or at least that section of the party in Canberra, and it is shared in varying degrees by both Labor and Liberal parties when they hold national office. It is the occupational hazard of being in government to believe that Canberra knows best, particularly the executive branch. Such a view leads to hostility towards any institution that checks the partisan ambitions of the government of the day — which is precisely why such limiting institutions and an entrenched constitution exist.

I should also mention the regional bias against federalism found in New South Wales. Recently in Sydney I was reminded that the most parochial newspaper in Australia is the *Sydney Morning Herald*. On occasion it will concede that Melbourne exists but generally the paper gives the impression that no Australian news occurs outside New South Wales, which, of course, includes Canberra. This reflects the view of most residents of the State that there is no need for federalism because New South Wales is Australia.

The Fallacies of Centralism

This aside, I am concerned not with criticisms of federalism, but with criticisms that the federal system is not working as well as it should. So, with the exception of a design fault in the Commonwealth Constitution to which I shall refer later, and

which has proved to have major consequences for the operation of the federal system, the answer to the question of whether there is anything wrong with the design of the Australian federal structure is, by and large, 'no'. This has been the opinion of the Australian electorate which has rejected all but eight of the 42 constitutional amendments submitted to the people since federation, and none of the successful amendments has affected the basic structure of the federal system. The compromise worked out to establish the federal union of 1901 has all the features that permit the benefits of a federal system of government to be fully exploited. The problem has been that in practice, and with more than a little help from the High Court, the creative tension inherent in the federal system has been steadily eroded by the increasing involvement of the central government in areas outside its intended jurisdiction. This has had two very bad effects.

The first is that it increasingly denies the opportunities for the States as political communities to find solutions to their own distinctive problems. Even though the Australian States and Territories vary less in their socio-economic composition than the components of most federations, the States have substantially different needs and face markedly different problems. The economies of South Australia and Victoria, disproportionately dependent as they are on tariff-protected industry and suffering a decline in relative population size, differ substantially from the resource and technology driven economies of Queensland and Western Australia. Besides, the much commented-upon similarity of State populations is changing rapidly with immigration and economic growth so that the States are diverging in their social and economic profiles.

A related aspect of the bad effect of greater uniformity is that it prevents the application of a range of solutions to problems that are common to all States. In some respects, it is the denial of experimentation in the solution of similar problems that is most worrying. Over recent years that has been constant reference, usually on the part of the Commonwealth government, to the need for national solutions and uniform laws to deal with a wide range of problems. This has ranged from demands for the same blood-alcohol limits for drink-driving laws, to pressure for a uniform national school curriculum. While there may be some cases where a single set of rules is justifiable, the unstated assumption is that national uniformity is intrinsically desirable. The fact that a problem is common to all residents of Australia has been taken as evidence that a uniform solution is required. We are all Australians, goes the call from the Commonwealth, so the same rules should apply to everyone.

This is as illogical as it is self-serving. It is true that the issue of providing the most appropriate health and education services, transport and water infrastructure, zoning and environmental laws are common to all Australians throughout the federation, but it is not true that there needs to be a single solution. Different communities have different preferences and the whole point of living in a free society is that we can devise institutional arrangements that permit diversity to flourish. Only in this way can we exercise choice effectively and feel that we are participating in shaping the decisions that affect our lives. If one community wants to spend more

on public health and less on education than another, why should this be prevented? If community standards vary, why should not communities vary in the rules governing criminal behaviour? Another way of framing the issue is to ask why uniformity should be preferred to diversity if communities find equally satisfactory but different solutions to the same problem.

A related fallacy is that these complicated issues have one single best solution. There is no one best way to provide education or health care. There are many solutions reflecting differing tradeoffs between the many considerations involved. It is not only undemocratic to prevent communities from finding their own solutions to these problems, it is also inefficient. To prevent diverse solutions is like preventing car manufacturers from producing different models, or drug companies from trying new drugs, or publishers from publishing different books. It is an arrogant denial of the need for experimentation to cope with a constantly changing world and to keep government services responsive to the communities they serve.

But, some will say, what about national standards? Isn't it important that there is general agreement on policies which have large spillover effects beyond the limits of any one State? Yes, but if uniform rules are to be preferred to deal with a particular problem, the way in which uniformity is achieved is itself important (note Pental, 1996). Uniformity can be imposed or be the consequence of a negotiated solution. Unfortunately, the Commonwealth is often in the position to force uniform solutions on the States, usually through financial pressure but sometimes through the extensive ambit given to its constitutional powers by the High Court. However derived, the ability to impose a uniform solution is guaranteed to produce a less satisfactory solution than a negotiated one, and on most occasions no solution is preferable to an imposed solution. Much of the justification for unilateral Commonwealth action is driven by the rhetorical ploy of arguing that any solution is better than none, even though those who have the responsibility of administering the solution are happy to live with the existing problem. The Commonwealth, for example, argued that there was a need for uniform blood-alcohol limits for drink-driving laws but, when pressed on the conflicting evidence about the effect of differing blood alcohol limits, could only point to the lack of uniformity as the problem that was to be overcome.

To begin with, a negotiated solution will involve compromise and will secure wider agreement than an imposed solution which only has to please the dominant party. Second, the framing of policy is a highly complex task and likely to generate unintended consequences and costs. Negotiation makes the process of policy formation less error prone and reduces risk. Third, by involving a wider range of interests in the final decision, negotiation ensures that decisions are given greater authority and legitimacy. These attributes are axiomatic, but they are well documented in the effect that the Senate has had in vastly improving the operation of the legislative process in the Commonwealth Parliament through the Senate's ability to force compromise. Of course, negotiation may slow down the process of framing policy and may offend the partisan or bureaucratic certainties of the instigating agency. But these costs to the would-be dominator are benefits to everyone else.

There is an added reason why solutions imposed by the Commonwealth on the states are particularly unsatisfactory. The States are the dominant agency in the provision of services and the day-to-day administration of the machinery of government. The Commonwealth may have the money, but the States have the practical knowledge and administrative experience in delivering the service. This means that Commonwealth-State transactions that are dominated by the Commonwealth, and particularly those that are driven by conditional grants, are likely to take the form of unequal bargains in which the States feel they are constrained to take note of programme specifications produced by a Commonwealth agency that has little practical knowledge of the problems faced by the state agency. This is quite apart from the fact that each agency has political priorities that are likely to diverge. Such a situation provides strong incentives for the State agency to try to circumvent grant conditions, and equally strong incentives for the Commonwealth agency to impose ever stricter conditions, performance indicators and auditing requirements on grants.

This spiral of cheating and checking generates the kind of bureaucratic nonsense that is the bread and butter of intergovernmental relations. It is the reason why trying to implement policy through conditional grants guarantees that real political problems are likely to be ignored in favour of the meta-politics of bureaucratic competition and rent-seeking. I am not arguing that all Commonwealth-State agreements are doomed to be ineffective and wasteful, just those where the negotiations are one sided in favour of the Commonwealth. Unfortunately, the bulk of intergovernmental relations in Australia is driven by the financial dominance of the Commonwealth and this is precisely the circumstance that produces the most dysfunctional outcomes.

Restoring Genuine Intergovernmental Competition

So much for the wickedness of attempting to impose uniform solutions on problems which require diverse answers or negotiated settlements. But this is only one of the bad effects of the involvement of the Commonwealth in areas outside its administrative competence. The other bad effect is the reduction of competition in the federal system.

This sounds like a paradox because, if the Commonwealth is involved in areas which are the concerns of the States, there ought to be more competition, not less. It has often been noted that the concurrent nature of most Commonwealth powers, and the use of Commonwealth financial muscle to influence policies in areas of state responsibility, has meant increased competition and increased responsiveness in the system as a whole because of the competition between State and Commonwealth government and the greater number of access points for interest groups. The overlap and duplication of government activity between State and Commonwealth agencies may create some waste, but the overall effect is to add, as a colleague of mine put it, 'extra vitamins' to the policy process (Painter, 1988). This is a view I used to hold myself until I looked at the nature of the competition that was being created, or, rather, not created.

Competition implies the ability to compete on a reasonably equal footing in a context where similar rules apply to the competing parties. With a few exceptions, this is not the nature of Commonwealth-State competition in areas where both governments are involved in framing policy. There are two reasons for this. The first is that the High Court has interpreted Section 109 of the Commonwealth Constitution in a way which strongly favours the Commonwealth. This section provides that a valid Commonwealth law overrides a State law to the extent of the inconsistency, and the High Court has held that almost any Commonwealth law in a given field overrides any State law in the same area even if it is possible to obey both laws, or if the State law deals with matters beyond the concern of the Commonwealth law. This has had the effect of giving the Commonwealth a very substantial advantage in any policy area in which it has jurisdiction, and has discredited the notion of concurrency.

The second and much more important reason is that the Commonwealth usually gains involvement in a policy area by offering funds to the States in return for political influence. As the States are already dependent on the Commonwealth for more than half their funds, and have become accustomed to assuming that they should never refuse any money offered by the Commonwealth, the nature of the negotiations is fairly one-sided. This is not competition but exploiting market dominance. The States are able to fiddle the details of most intergovernmental arrangements to suit State priorities, but this is hardly a ringing endorsement of increased competition in the federal system. At best it is cooperation under mild duress and at worst coercion modified by State ability to undermine the agreement by administrative deception.

There are some occasions where effective competition occurs between the States and the Commonwealth, but the prerequisite is that money is not the most important issue on the table. The recent negotiations over gun laws, for example, are a case in point. There was real competition in the sense that each State government had complete control over gun laws within its territory, and the Commonwealth had control over the importation of guns. The result was genuine compromise because no government could be coerced by another within the area of its jurisdiction. This is another paradox: the basis for effective competition, in the sense of the potential for the maintenance of different policy solutions to the same problem, is the most effective basis for compromise and the achievement of genuine cooperation.

But there is a more serious aspect of the loss of competition that follows from increasing Commonwealth intrusion into State administrative concerns. This is the reduction in the ability of States to compete in the provision of services where diversity can be of national benefit. One of the best examples of this is the administration of university education, an area clearly outside the Commonwealth's original jurisdiction. Since 1974 the Commonwealth has bought effective control of university education from the States by relieving them of the need to pay for universities. While universities are still State institutions governed by State laws, the Com-

monwealth has secured, through a range of financial measures, close to monopoly control of the whole tertiary sector.

This dominance by a single government funding source has had a seriously debilitating effect on university education in this country. Quite apart from the question of the level of funding, Commonwealth control has killed much of the experimentation and diversity that is the life blood of a university system and that is required if the university sector is to serve the national interest in both teaching and research. As the West Report has put it, the Commonwealth regime has provided 'greater incentives to be the same rather than different' (HEFPRC, 1997:19). University administrators and academics spend too much of their time conforming with performance indicators, enrolment profiles and similar regulations that have more in common with the former communist regimes in Eastern Europe than with a free society. The idea that universities should be enterprises that make their own decisions and take responsibility for the level and variety of their fees, for the number of students they enrol and the courses they teach, seems not to have dawned on the Commonwealth government, even though it is the kind of solution that the Commonwealth has favoured for most other areas of government enterprise. Eight autonomous State and Territory university systems would not guarantee that no mistakes would be made, but it would mean that there would be much more diversity and resilience in the university sector, and that disasters were quarantined rather than affecting the whole system. Such a dispersed system of public universities is one of the reasons why the Canadian university system is much superior to ours.

Prospects for Reform

So much for the diagnosis. Our federal system is not working properly because of a loss of diversity in the system, a diversity that enhances creative competition and makes for greater responsiveness to citizen preferences, greater efficiency, and greater resilience in coping with national problems.

How can this situation be remedied? The answer is, with difficulty. The problem is that all the incentives are pointing the wrong way. The Commonwealth has no reason to reduce its involvement in any policy area in which it finds political gain, and the States are apprehensive about any changes that would force them to take more responsibility for raising taxes. For a while in the early 1990s, Prime Minister Hawke and a series of special premiers conferences gave the impression that some progress would be made. The States were to regain greater autonomy in some policy areas, while the Commonwealth would pick up more control in others. But the key element was greater financial autonomy for the States, and it was this proposal which attracted the ire of Mr Paul Keating. After Mr Keating's successful leadership challenge, the proposal sank without trace.

In the short term, the only real remedy is a financial one. Currently, the States raise less than half the revenue they spend, the remaining funds being transferred from the Commonwealth. The States need to be able to say 'no' to any Commonwealth involvement driven by financial inducement, and they can only do this if they can feel secure about the source of their funding. This security requires the States

to have direct access to the major fields of taxation revenue from which they are presently excluded: consumption taxes and income tax. The High Court, through its idiosyncratic interpretation of Section 90 of the Commonwealth Constitution, has precluded states from raising taxes in the nature of retail sales taxes on goods, so State consumption taxes are not the answer. The States are currently discussing a number of proposals relating to Commonwealth-State finance, one of which is a Commonwealth-levied consumption tax, a fixed share of which is guaranteed to the States. But this cannot create long-term independence, partly because the States cannot control the levying of the tax and partly because such agreements can be revoked at the convenience of the Commonwealth.

If the States resumed access to personal income tax from which they have been, in practice, precluded since 1942 (Sharman, 1993), this would create a very different picture. If the whole field of personal income tax were taken over by the States, as was considered in the 1920s, there would be little need for any Commonwealth transfers. This would create competition with a vengeance, even if the income tax schedule and the rate of tax levied by the States were identical. It would mean not only vastly greater policy discretion for the States but also the end of all those Commonwealth departments such as health and education whose existence is dependent on monitoring Commonwealth transfers to the States. There would be no more premiers' conferences on finance as we know them because the States and Territories would be largely self-sufficient in revenue. There would still be discussions about borrowing, and additional negotiations about equalisation payments to the poorer States and Territories, but the main feature would be deep and meaningful discussions about the state of the economy and what State, Territory and Commonwealth governments could do jointly to regulate it.

Such a change would create a federal system with all the dynamics required for a highly responsive and effective political system but there are many reasons why such wholesale change, however desirable, is unlikely. The first is that the Commonwealth would be the big loser in both power and prestige. Another set of losers would be all those interest groups that depend on Commonwealth patronage in areas of State responsibility. This is now a very large and influential set of lobbyists. Even the big winners under such a system, the States, would be extremely apprehensive about such a revolutionary change. Not only would it require much greater State administrative responsibility for the framing of policy, but it would require a willingness to accept political responsibility for all aspects of State expenditure. While this would be wholly beneficial for State citizen voters, it would require a major change in mind-set for most State governments. They may complain about Commonwealth interference, but the thought of being completely responsible for health and education policy, for example, and for the raising of the tax to pay for these services, is likely to make them turn pale.

But the Canadians have shown that a half-way house is quite possible. Both spheres of government in Canada are involved in raising personal income tax on the same schedule, with minor variations in the rate of tax. Transfers to the Provinces remain in those areas of key concern to the central government, but the Provinces

retain considerably more financial independence than the Australian States. I hope the premiers will support a similar scheme in the current round of discussions on federal finance, but I fear that Commonwealth intransigence and State faint-heartedness will defeat such a reform. The States are still suffering from the view, mistaken in my opinion, that if a State opposition party mentions the words 'double taxation', any government that supports a State income tax will be defeated by the kind of huge swing that New South Wales premier Neville Wran gained using this slogan in the late 1970s. As Sir Humphrey would say, a courageous decision is required.

State-Initiated Constitutional Amendment

Of course, we could try for a long-term solution to the problem. This brings us back to the design fault in the Commonwealth Constitution. At the moment, the only way that changes can be made to the formal structure of the Constitution is through changes initiated by the Commonwealth Parliament and accepted by the Commonwealth government before being put to the people at a constitutional referendum. This initiation procedure denies to the States the opportunity of proposing alterations to the Constitution. This is a serious omission because it denies voters the opportunity to express an opinion on proposals for constitutional amendment which might limit Commonwealth power, something the Commonwealth government is never likely to submit to the voters. My preference would be for an additional initiation process for constitutional change which could be set in train by a proposal for constitutional amendment being passed as a resolution by a majority of State legislatures. Such a proposal would then be required to be submitted to the people at a referendum and, if it gained the necessary majorities, would amend the Constitution.

Such a procedure would, at the very least, enable the electorate to pass judgment on the changes that have been made to the federal system by stealth. All these changes, whether deriving from judicial interpretation or from financial pressure, have worked in the direction of reducing State autonomy and increasing the ambit of a centrally initiated uniformity. A State-initiated constitutional amendment process could act as a vital corrective to the drift away from the diversity that underpins a successful federal system — and the betting is that such a procedure would greatly increase the success rate of constitutional amendments because the proposals would be the result of a process of intergovernmental compromise rather than the preferences of the Commonwealth cabinet.

But what about the title of this paper? How can I conclude without reinterpreting it so that it corresponds with what I have been talking about? The solution is to say that working together can take place effectively only if we know we can choose to work separately. We must be free not to work together, otherwise joint action is a form of slavery. The potential for serious conflict is the best argument for fruitful cooperation. The whole point of this paper is that the autonomy of the various political communities that comprise the federation is a vital prerequisite for the responsiveness and efficiency of the governmental system as a whole.

As for an inclusive federalism, perhaps that is best left as a contradiction in terms or, as Sam Goldwyn said, '[ladies] and gentlemen, include me out'.

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From Welfare State to Optimal Size of Government: A Paradigm Shift for Public Policy

Patrick J. Caragata

NEW ZEALAND has climbed a tax mountain for most of the 20th century. In 1921 the total tax take exceeded 15 per cent of GDP; in 1941 it exceeded 20 per cent; in 1943 25 per cent; and in 1980 30 per cent. In 1990 it reached a historic peak of 36 per cent, falling back to 34 per cent in 1997.¹

This tax mountain is the creation of rising government expenditure. In 1973-74, government expenditure accounted for 28 per cent of GDP. After 1975, it generally remained over 38 per cent and peaked in 1986-87 at 44.2 per cent. Much of this increase reflected the rising cost of social transfers, which jumped from 12 per cent of total government expenditures in the early 1970s to a peak of around 22 per cent in 1989.

During 1950-75, interest on the public debt averaged 2.4 per cent of GDP a year. It rose to 3.2 per cent in 1975-79, 5 per cent in 1980-84, and 7.2 per cent in 1985-89. It peaked at 8 per cent of GDP (and 20.7 per cent of government expenditure) in 1987-88. This level was comparable to the early years of World War II (1940-42), when interest payments consumed 22.4 per cent of total expenditures. The gross public debt itself was 40.5 per cent of GDP in 1973-74; within five years, it reached 53 per cent of GDP. At its peak in 1986-87, the gross public debt reached 77.2 per cent of GDP.

Even in the late 1980s, after the reforms of Roger Douglas, the Minister of Finance, government expenditure did not fall below 38 per cent of GDP, ten percentage points above the 1973-74 level. The ratio remained at 38 per cent for the first two years of the Bolger National government (1991-92), reflecting the need to cushion those most affected by the structural adjustment of the economy and high debt service payments (Caragata, 1997:55-70).

This huge increase in the role of government, from 28 per cent to 44 per cent of GDP in the 13 years from 1973-74 to 1986-87, was not planned; nor was it subjected to any cost-benefit analysis or risk assessment of its potential impact on the

¹ This estimate excludes local government taxes and the Accident Compensation Commission levy that together account for 3 per cent of GDP.

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economy. Rather, it reflected a dominant welfare-state paradigm about the role of government that has guided political thinking for over 50 years but is now beginning to lose its grip.

The main aim of this article is to summarise some recent research findings on the rising paradigm on the optimal size of government that is replacing the welfarist paradigm.

The Rise and Fall of the Welfare State Paradigm

As understood by Thomas Kuhn (1962/1970) in his study of scientific revolutions, paradigms are frameworks of concepts and assumptions that organise and explain experience. Over time, anomalies accumulate that become too difficult for the reigning paradigm to resolve; eventually it breaks down and is replaced by a new paradigm.

J. M. Keynes is a central figure in the emergence of the welfare-state paradigm, which he elaborated by rejecting the two extremes of state socialism and *laissez faire* and defining a middle ground between them. This new paradigm sanctioned 'the enlargement of the role of government' for the purpose of correcting deficient demand (Keynes, 1936:380-1). The problem with the new paradigm was that it consisted of the middle ground between two extreme options in an extreme case: the Great Depression. After the Western economies recovered, growing liberalisation of international trade and (later) of capital flows challenged the role and competence of government's economic management. Eventually, the welfare state reached its limit in the 1990s, when fiscal deficits and public debt grew to proportions that destroyed government's ability to intervene effectively: additional government spending raises interest rates, which negates any stimulus it provides to demand.

The welfare state was seen as a political and social panacea by the post-war generation (the 'baby-boomers') who were the first beneficiaries of the full range of its services in health, education and social security, as well as by an older generation that benefited in particular from the old-age pension. Even as it was being stretched far beyond its original purpose and problem-solving capabilities, it became closely identified with democracy itself. But then it started to undermine welfare by weakening the values and protective power of the central institutions of civil society: the family, the churches, and the voluntary associations.

This problem has led Sandel (1996:3) to identify the two principal causes of what he calls *Democracy's Discontent*

One is the fear that, individually, and collectively, we are losing control of the forces that govern our lives. The other is the sense that, from family to neighbourhood to nation, the moral fabric of community is unravelling around us. These two fears — for the loss of self-government and the erosion of community — together define the anxiety of the age. It is anxiety that the prevailing political agenda has failed to answer or even address.

Sandel (1996:351) ends his book by observing that 'the hope of our time rests ... with those who can summon the conviction and restraint to make sense of our condition and repair civic life on which democracy depends'.

Yet despite his valuable insights, Sandel fails to see the connection between large, intrusive government and the loss of autonomy and the erosion of community. As taxes rise and the government gets bigger, it tends to crowd out the institutions of civil society by pre-empting their roles and undermining individual self-reliance. This argument was made by Alexis de Tocqueville (1835/1945:116) over 150 years ago, in an astonishing premonition not only of the rise of the welfare state but also of the problems that have brought it into question:

The more [government] stands in the place of associations, the more will individuals, losing the notion of combining together, require its assistance: these are causes and effects that unceasingly create each other ... The morals and the intelligence of a democratic people would be as much endangered as its business and manufactures if the government ever wholly usurped the place of private companies.

Government has a role to play in assisting those in genuine need. But should as many as a fifth of New Zealanders of working age, and nearly a third of New Zealand's children, be dependent on state welfare (Cox, 1998:27)?

Paradigm Shift

There are numerous signs that the tide of big government is receding. Interest is growing in the high compliance costs of government. The appearance of Osborne and Gaebler's book *Reinventing Government* (1992) suggests that governments are trying to increase the efficiency of public spending. In his 1996 State of the Union Address, US President Bill Clinton announced that the 'era of big government is over'. In the late 1990s, there is talk, and even some action, in the United Kingdom, the United States, Australia and New Zealand on replacing welfare handouts with 'workfare'.

The principal reason for this disillusionment with big government is that, if it grows beyond a certain point, the public sector reduces welfare rather than increases it. In his overall analysis of the link between taxes and growth, Gerald Scully, a leading pioneer in the field of the optimal size of government, has observed that:

Economic theory suggests that up to some level, government expenditures increase the productivity of private economic resources. The provision of national defence and a judicial system protect private property and individual rights. Other publicly provided goods, such as infrastructure, also enhance private productivity. Thus, up to some point, government expenditure acts as a positive externality on private economic activity ... Beyond some optimal size of government, increased taxation acts as a negative externality on the private sector. (Scully, 1996a:4-5)

The new paradigm therefore centres around the question: what is the optimal size of government? Martin Feldstein (1996:26) has recently argued that 'the central public finance question facing any country is the appropriate level of spending and therefore of taxes'. A considerable literature has emerged that attempts to answer that question. Clark (1945), inspired by Keynes, suggested that where the objective is to minimise inflation and stabilise the exchange rate, the optimal effective tax rate is likely to be around 25 per cent of national income (equivalent to about 21 per cent of GDP in New Zealand). More recently, Peden (1991:168-9) has found that over the period 1929-86 US government expenditure up to 17 per cent of GNP improved the productivity performance of the economy, but expenditures above that level reduced 'the growth of productivity'.

In its 1997 *World Development Report*, the World Bank (1997:168-71) emphasises the value of an 'effective state' that facilitates rather than impedes higher levels of economic performance. Its cross-country study examining the impact of 14 independent variables on the growth in GDP per head concludes that the size of government (measured by government consumption's share of GDP) has an important and consistently negative impact on the standard of living (though it did not search for an optimal level of tax or expenditure relative to GDP).

Tanzi and Schuknecht (1997) compare the economic performance (growth rates, gross fixed capital formation, inflation, unemployment, and debt) and social performance (life expectancy, infant mortality, education and income distribution) of 17 small, medium and large OECD countries. They conclude that 'there is no evidence' that countries with big governments out-perform the countries with medium and small governments. When government expenditure rises much above 30 per cent of GDP, there are diminishing returns to the social gain from public spending (Tanzi & Schuknecht, 1997:167).

Finally, a recent OECD report has concluded that:

up to one-third of the growth deceleration in the OECD (from around 5 per cent in 1965-73 to around 2 per cent in 1989-95) would be explained by higher taxes. In some European countries, tax burdens increased much more dramatically than the OECD average, which would imply correspondingly larger effects on their growth rates. (Leibfritz, Thornton & Bibbee, 1997:49)

Optimal Tax Levels for Growth and Employment

Caragata (1998) presents the final report of the New Zealand Inland Revenue's Taxation Economics Group. One of the principal aims of our research project during 1994-97 was to determine the level of tax that is optimal with respect to two simultaneous objectives: (i) maximising economic growth and employment; and (ii) efficiently minimising tax evasion. Our approach was to estimate a range for the ratio of tax to GDP and the tax mix (direct and indirect tax relative to GDP) that would maximise economic growth and employment and efficiently minimise tax evasion.

For New Zealand, we concluded that the optimal level of total tax (the level at which economic growth is maximised) is probably located between 15 per cent and 25 per cent of GDP. We used five separate sets of models, with three research teams. This multiple-methods approach was designed to provide reassurance about the quality of the results.

Scully (1996a) uses a non-linear Cobb-Douglas production function model that combines analysis of the tax mix, the ratio of tax to GDP and the rate of real economic growth. The model can also be used to estimate the tax burden and tax mix that maximise employment growth and economic growth, and minimise deadweight loss. The model involves an economy with a public sector and a private sector, exhibiting constant returns. The latter feature of the model is supported statistically by the data. With this constraint, and using the empirical estimates for the model's parameters, positive growth paths emerge. The empirical basis of the model is crucial: misleading results could be obtained if arbitrary values were assigned to the parameters. The rate of growth is a function of the tax level, and the model facilitates a calculation of the value of the latter rate that maximises output growth.

Scully (1996a) estimates that New Zealand loses two percentage points of growth a year because total taxes were higher than 20 per cent of GDP. His model yields a growth-maximising tax level range, covering the years 1927-94, of 16.4 per cent to 23 per cent, for an average of 19.7 per cent of GDP. Scully also finds that the growth-maximising tax levels for some other countries are consistent with those for New Zealand.²

Research by Scully (1996c) covering the period 1951-94 in New Zealand indicates that a one percentage point increase in the ratio of tax to GDP appears to have its strongest impact in labour markets on employment growth, although the impacts on labour force participation and the unemployment rate are also strong. A one percentage point increase in the ratio of tax to GDP in New Zealand lowers employment growth by over 42,470 workers, decreases labour force participation by 11,900 workers and increases the unemployment rate by about 15,900. The optimal tax level for maximising employment is about 20 per cent of GDP.

Deadweight Loss Estimates

Ballard and Fullerton (1992:118-19) note that deadweight loss analysis has typically ignored the effects of administration costs and compliance costs. By contrast, the work for New Zealand's Inland Revenue by Scully (1996a), Caragata and Small

² For the period 1927-88, the growth-maximising tax level for the UK was 25.2 per cent; the optimal level was lower for Denmark (18.5 per cent), Finland (18.9 per cent), Italy (20.1 per cent), and Sweden (16.6 per cent). The average across all the countries was estimated to be 19.9 per cent. In another paper on the growth-maximising tax level for the US, Scully (1995) estimates that, over the period 1929-89, real growth rates in the US decline when the ratio of tax to GDP rises beyond about 23 per cent. Earlier, Scully (1991:2) showed that for 103 countries for the period 1960-80 'on average, countries reach their maximum economic growth rates when they take no more than 19.3 percent of GDP in taxes'.

(1996a) and Branson and Lovell (1997) picks up these effects in their analysis of *dynamic* deadweight loss.

Branson and Lovell (1997), using a two-tier model employing both econometrics and data envelopment analysis, conclude that for the period 1946-95, on average, economic output fell short of its annual potential by 17 per cent because taxes were at 35 per cent of GDP rather than a growth-maximising rate of 22.5 per cent of GDP. This 'deadweight loss' is the gap between actual and potential economic performance arising from taxes.³ Branson and Lovell conclude that if deadweight losses were added to the existing tax burden, the effective tax rate would be 51 per cent of GDP, not 35 per cent.

Scully (1996a) estimates that, for each dollar of tax in New Zealand, there is a long-run cost to the economy of about \$2.70. The magnitude of these results is confirmed by Caragata and Small (1996a) and anticipated by Usher (1991), Bird (1991) and Feldstein (1995). These magnitudes are also consistent with the cumulative aggregation of output losses imposed by government intervention anticipated by Mancur Olson (1996). Thus, a cost-benefit analysis approach to tax policy-making would operate on the assumption that, for a dollar of government spending to be justified, it would have to produce a long-run benefit of at least about \$2.70.

Optimal Tax Levels for Efficiently Reducing Tax Evasion

Another approach to estimating the optimal size of the government is to determine the tax level that efficiently minimises the hidden economy and tax evasion. Twenty-five ago, when OECD countries' tax levels were averaging about 30 per cent of GDP, various studies estimated that their hidden economies ranged from 7 per cent to 16 per cent of GDP.⁴ Thus, an average of about 10 per cent of the income of OECD countries was unreported for tax purposes.

Currently, with the average ratio of tax to GDP of about 38 per cent, many countries have underground economies ranging from 10 per cent to 25 per cent of GDP, with an average at about 16 per cent. That is to say, while their average tax burden has gone up by 30 per cent since 1970, their hidden economies grew by about 60 per cent. For New Zealand, the tax burden rose by 35 per cent between 1971 and 1994, while the hidden economy jumped from 7 per cent of GDP in

³ This output efficiency approach is different from the conventional approach which emphasises the static allocative efficiency effects of tax. Thus, Diewert and Lawrence (1994, 1995) estimate deadweight losses in New Zealand of 18c per dollar of tax on labour, and 14c per dollar of tax on consumption, using a static model with no confidence intervals. For an econometric critique of these results, see Small (1995).

⁴ Giles (1996:7) summarises the hidden economy estimates for the 1970s. Recent research undertaken by Friedrich Schneider (1997) estimates the hidden economy at about 7 per cent of GDP in Switzerland and Austria, 12-15 per cent in Japan, the US, Britain, Australia the Netherlands, Germany, France, Canada, Ireland, Denmark, Norway and Sweden, and 18-26 per cent in Belgium, Spain and Italy. See also Aigner et al. (1988).

1970 to 11.3 per cent in 1994, an increase of 63 per cent (Giles, 1996). Thus, New Zealand's tax burden and hidden economy have been growing as fast as, or faster than, the OECD average. This raises the question of what ratio of total tax to GDP efficiently minimises the hidden economy and related tax evasion.

Five models developed by Giles (1996) show that the hidden economy responds more to tax than to inflation and government regulation, and that the hidden economy was pro-cyclical rather than counter-cyclical. In New Zealand, the hidden economy is currently around 11 per cent of GDP and tax evasion is estimated at about \$3.2 billion a year. As taxes are reduced, the hidden economy will shrink. But if taxes are driven to zero, the hidden economy will still be about 4 per cent of GDP, representing the hard core of criminal activity in the hidden economy that is driven by factors other than tax (Giles & Caragata, 1996).

Caragata & Giles (1996) develop a model for New Zealand estimating an efficient tax evasion-minimising optimal tax level of 21 per cent of GDP. This provides further corroboration that the optimal tax level is close to 20 per cent of GDP. We find that a mix of 33 per cent direct tax and 67 per cent indirect tax would most efficiently minimise the size of the hidden economy and tax evasion. We conclude that if the tax department adopts scientific audit selection,⁵ there would be significant tax revenue gains and significant savings in terms of administrative efficiency for the tax department and compliance cost savings for business.

The Optimal Tax Mix

Two models that we developed for New Zealand with a growth-maximisation objective favour a tax mix that emphasises direct taxes. Another model with a similar objective emphasises indirect taxes. A fourth model with an objective of minimising tax evasion emphasises indirect taxes.

All the models indicate that the total tax burden is far more important than the tax mix in its impact on economic growth and tax evasion. Branson and Lovell (1997) conclude that the level of tax is six times more important than the tax mix in influencing growth. Scully (1996b) concludes that a mix of 57 per cent direct tax and 43 per cent indirect tax would maximise economic growth at a tax:GDP ratio of 20 per cent. Branson and Lovell (1997) conclude that, on average, a mix of 65 per cent direct tax and 35 per cent indirect is optimal for promoting economic growth in New Zealand at an average optimal tax:GDP ratio of 23 per cent.

Caragata and Small's (1996b) non-linear model estimates that, with a ratio of tax to GDP of 20 per cent, tax policy would most accelerate economic growth when the tax mix is 28 per cent direct tax and 72 per cent indirect. This model finds that the relationship between growth and direct taxes is always negative: which implies that a tax mix of zero direct taxes and 100 per cent indirect taxes would potentially maxi-

⁵ Scientific audit selection ranks all taxpayers from lowest to highest risk and permits rational audit selection. This approach offers the prospect of significantly reducing audit compliance costs of firms which are typically compliant (by diverting audits to higher-risk firms), and reducing operation costs by permitting an efficient reallocation of audit resources to higher-risk firms.

mise economic growth. However, the Caragata-Small model is not free of measurement error and its conclusions are tentative and subject to caution despite their confirmation of the strong trend in economic theory favouring the abolition of the income tax.

Finally, Caragata & Giles (1996) find that a mix of 33 per cent direct and 67 per cent indirect would most efficiently minimise the size of the hidden economy and tax evasion.

While both the objectives of maximising economic growth and minimising the hidden economy suggest that the current tax mix favouring direct tax over indirect is less than optimal, it seems that a growth-maximisation objective suggests a frontier mix with a rough balance between the two. Thus, too much weight on indirect taxes in pursuit of reducing the size of the hidden economy could undermine economic growth. More research on these new findings is required.

Implications for Fiscal Policy

All countries have paid a high and often unseen price (in terms of reduced growth and employment and higher tax evasion) for climbing the tax mountain in pursuit of the objectives of the welfare state. The huge increase in the size of government that occurred mainly between the early 1970s and the late 1980s was a failure in economic development and policy management.

The old ideological paradigm of the welfare state is now beginning to give way to the empirically based paradigm of the optimal size of government. How can governments most rapidly incorporate the insights of the new paradigm into its fiscal policies?

Tax policy. The first priority is to cut income taxes so that the total tax burden falls and the tax mix places greater emphasis on consumption tax. Tax cuts have weaker growth effects at higher rates (such as 35 per cent of GDP) than at lower rates (such as 25 per cent of GDP). Tax cuts are also best applied before an economy falls into recession.

Crisis management. There is nothing wrong with counter-cyclical financing and government deficits as long as they occur only in emergencies and for short periods. Keynesian fiscal strategies became discredited because politicians wanted to run deficits even during boom times in order to buy votes.

Universality. End universal welfare benefits, which benefit the rich unnecessarily. Help those who need it. Means test all social services and programmes.

Transparency and accountability. Each year, all efficiency and benchmarking reports produced for government departments and agencies should be made public so that taxpayers can determine if they are obtaining value for money from their taxes.

Public choice: The public should be given more choice about how to spend their money. Many people who are dissatisfied with government provision of police, education and health services opt for private sector solutions, but cannot avoid paying taxes. Thus, they pay twice for these services when they opt for private provision of such services.

Timing: It took 40-50 years to push the state's share of the economy to its current level. It may take a decade or so to move taxes down to about 22-25 per cent of GDP, in part because of the need for a smooth transition. It should not be allowed to take much longer than that, because higher economic growth is needed in order to finance the expected increase in spending on health services when the retirement of the baby-boom generation peaks in 2025.

The culture of public control, or regulatory and intrusive management, that has grown up under the welfare state must be ended and replaced with the culture of public service that respects taxpayers as the shareholders of government. The greater the numbers demanding benefits from government, the greater is the welfare dependency of the population, and the greater the level of government control. The greater the level of control, the less acceptable and the more wasteful are government services likely to be. Reducing taxes helps to encourage less wasteful spending and greater personal responsibility.

The new paradigm of the optimal size of government offers politicians the basis for addressing 'democracy's discontent' by reducing the culture of dependency arising from the intrusive welfare state and promoting self-development and learning as the basis for national re-invigoration and enhanced international competitiveness.

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The Political Economy of the Kyoto Protocol

Aynsley Kellow

MUCH writing on the international politics of the environment might suggest that the threat of climate change makes a consideration of national interests somewhat redundant, since, in the face of a common threat, global interests override the interests of states.

Such a belief may be at least partly responsible for the widespread disappointment with the results of environmental policy-making at the international level which was so much in evidence at the 1997 United Nations General Assembly Special Session convened to review progress on the agenda adopted at Rio de Janeiro in 1992 (Sandbrook, 1997). The challenge is no longer to conclude multilateral environmental agreements (MEAs), but to conclude MEAs that are going to deliver positive environmental outcomes. Too often, MEAs have been developed in considerable ignorance of important national interests by delegations to international negotiating meetings at which environment agencies and interests are represented but those of industry and trade are not. It is not surprising that commitments are not honoured in ratification and implementation, and are undermined by domestic policy processes in which interests less influential at the international level are able to extract redress at the expense of reducing MEAs to mere symbolic gestures (Kellow, 1997). While excluded or marginalised in the processes by which MEAs are developed, business is more influential at the level of domestic politics, enjoying what Lindblom (1977:170-88) saw as the 'privileged position of business' thanks largely to its role in delivering investment.

International environmental policy requires states to assume responsibilities, and to undertake actions to give effect to those policies. Unlike domestic policy, new requirements cannot generally be imposed upon agents contributing to the causes of problems. For example, experience with the 1987 Protocol limiting the emission of ozone-depleting substances has shown that some nations are either unwilling or unable to deliver on international commitments, and a thriving black market has undermined the Protocol's effectiveness. Policy adopted in ignorance of significant national interests and important sectoral interests is thus almost certainly doomed to failure, and policy to deal with the risk of a rate of climate change which will tax the adaptive capacities of human and natural systems is no exception.

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It is therefore important to examine the interests involved in the development of the Kyoto Protocol.

Risk, Science and National Circumstances

In a political sense, the most significant winners and losers in relation to climate change policy are perhaps those affected by the policy rather than by the risk of accelerated climate change. The costs of climate change will be remote in time and interests affected by them poorly organised, but the winners and losers associated with the policies adopted are in the present and much better organised. But it is important to bear in mind that the assessment of the risk posed by accelerated climate change depends crucially upon the circumstances of national and sectoral actors. One's risk assessment differs substantially depending on whether one lives in a low-lying island state, or a state with substantial low-lying land such as Bangladesh or the Netherlands, or an elevated inland state (Adams, 1995). Risk assessment cannot be based upon science alone. It inevitably reflects differing national circumstances and subjective factors. Indeed, one of the problems with the Intergovernmental Panel on Climate Change (IPCC) process is that it seeks in many ways to make a risk assessment which the scientists involved are not qualified to make, and which should be left to the policy-makers. For example, the controversy over the attribution of past observed climatic change to human agency in the Second Assessment Report of the IPCC (Houghton et al., 1996) reflects tensions between the need to produce a scientific consensus and the national and sectoral interests of some participants: the US State Department played a role in revisions to downplay the uncertainty in the science, while fossil fuel interests raised these revisions as a political issue.

The view that a consensus must be produced, rather than allowed to emerge from traditional scientific controversy (as was the case with chlorofluorocarbons), presupposes that action will not be taken unless a consensus is manufactured, and thus presupposes that action is needed. Since climate science is based on models of the global climate system which are limited by the computational power of supercomputers, and so is unlikely to resolve the attribution controversy definitively, a risk assessment performed by the IPCC is likely to continue to be contested by those with different interests in the causes, effects, and solutions (see Kerr, 1997). But this is not only unavoidable: it is desirable. The key policy questions are about what costs we should accept to attempt to mitigate how much climate change, and on the basis of what degree of scientific certainty. Not only is science alone unable to provide the answer; neither can the precautionary principle (which states that lack of full scientific certainty should not be a reason for inaction), since it cannot tell us how much precaution we should exercise. Such questions are inescapably political, and inextricably bound up with questions of ethics and interests.

To assume that interests do not matter, and that the imperative of the IPCC scientific consensus and a common threat of climate change will produce an effective and workable international instrument to it, is to risk the whole ability of the international system to respond to the problem. Diverging risk assessments are

then likely to take over, at the cost not only of the loss of effective response to the risk of climate change, but an even further loss of faith in international processes and institutions. But since there are problems for which effective international capacity is needed, we need to develop a policy response which takes account of the political economy of the Framework Convention on Climate Change (FCCC) and the Kyoto Protocol adopted at the Third Conference of the Parties in December 1997.

Interests and Morality in Climate Change Policy

A basic difficulty in identifying the interests at stake in the FCCC is that they are confused by a moral cloak of equality which, paradoxically, is grossly unequal. One of the fundamental flaws with the FCCC, with which Australia took issue, is the egalitarian appeal which made agreement in Rio de Janeiro possible: the non-binding commitment of stabilisation of emissions at 1990 levels for Annex I nations (essentially the OECD countries plus Eastern Europe and the former Soviet Union) by 2000. Both the egalitarianism of that commitment (and of later calls for uniform reductions in emissions from the European Union (EU) and Alliance of Small Island States for Kyoto) and the use of 1990 as a base year were so unjust as to jeopardise any delivery on commitments.

It was Anatole France (1894) who wrote of the 'majestic equality of the law, which forbids the rich as well as the poor to sleep under bridges, to beg in the streets, and to steal bread'. The circumstances of nations differ hugely: levels of wealth, rates of population growth, rates of economic growth, energy-intensiveness of their economies, requirements for transport, heating and cooling, and energy sources available as the result of natural-resource endowments and past investment decisions. Any requirement which ignores these differences in the interest of a quick consensus-generating appeal to equality is doomed to fail.

The examples of the United Kingdom and Germany, which formed the self-interested basis of the EU position, reveal the injustice that can be masked by seemingly equal commitments. The privatisation of the UK electricity sector in 1990 and the subsequent demise of the coal mining industry resulted in a 'dash for gas' which made any reductions in CO₂ emissions much less difficult for the UK, since gas produces fewer emissions per unit of electricity generated; moreover, new combined-cycle generation lifts conversion efficiencies from the order of 40 per cent to around 50 per cent, reducing CO₂ emissions by 60 per cent compared with coal. The dash for gas was made possible also by the relaxation in 1990 of a 1974 EU Directive prohibiting the use of gas (as a premium fuel) for electricity generation, and by the need for the UK to limit sulphur dioxide emissions. (A similar 'premium fuel' policy in Victoria can be seen to have resulted in State-commissioned 3000MW of brown coal plant over the past decade which was only 25 per cent thermally efficient, thus producing more CO₂ per unit of electricity.) UK gas plant capacity and generation now account for about 20 per cent of all fossil fuel capacity and generation (Bantock & Longhurst, 1995), resulting in a windfall

emissions reduction, unrelated to climate change policies, of about 12 per cent in the electricity sector since 1990.

Germany was particularly advantaged by both the uniform targets approach and by the selection of 1990 as the base year. German reunification occurred in October 1990; over the following year, economic activity in the former East Germany contracted by 23 per cent and total primary energy consumption declined by around 30 per cent (Boehmer-Christiansen et al., 1993). Ironically, some European nations such as the Netherlands and Denmark were disadvantaged by the selection of 1990 as a base year, because climatic conditions that year gave them an abnormally low level of energy use and thus greenhouse gas emissions as a target.

The 'European bubble' proposal involved setting a single reduction target for the EU, while allowing different targets for each member nation. It thus allowed the serendipitous gains of Germany and the UK to be offset against the excesses of Greece and Portugal, which were to be permitted to increase their emissions by around 30 per cent and 40 per cent respectively. Luxembourg was to have reduced its emissions by 30 per cent, but it can import energy — as can much of Western Europe (Sweden is laying an undersea cable to Poland, for example). But the issue raised by the European embrace of differentiated responses is not only that it was unjust that the EU alone should differentiate, but that, if political agreement within an organisation such as the EU, with its single market and a planned single currency, required recognition to be given to the different national circumstances of its member states, what real prospect was there of worthwhile multilateral agreement being secured *without* differentiation?

Agreement among Annex I Parties in Kyoto was secured only after acceptance of the need for differentiation by Japan and (eventually) the US. Russia offered to trade its windfall emission reductions, and the US negotiators fashioned a bloc based around Annex I members of the Asia-Pacific Economic Cooperation (APEC) group, which Russia had joined only the previous week, crafting an 'umbrella' of differentiated responses to counter the EU bubble. The negotiation took on all the appearances of a trade negotiation and only an outcome which took account of differing national interests was possible. The agreement included differentiated responses from Annex I Parties, with the net effect that their aggregate emissions of the six most important greenhouse gases would be reduced by at least 5 per cent below 1990 levels in the budget period of 2008-2012. The EU was required to reduce emissions by 8 per cent below 1990 levels, the US by 7 per cent, and Japan by 6 per cent; while, in addition to increases by individual nations within the EU (Greece, Portugal, Spain, Ireland, Sweden), increases were allowed to Australia (8 per cent), Iceland (10 per cent) and Norway (1 per cent). The agreement also provided for emissions trading, details of which were to be determined at the Fourth Conference of the Parties in Buenos Aires in November 1998.

The Kyoto outcomes are relatively modest, but they are steps towards the development of workable policy instruments that have some prospect of being ratified and honoured (although it must be acknowledged that US ratification is problematic, and Annex I Parties will be looking to Washington before they act). Kyoto

represents the failure of the 'blame and shame' tactics adopted by non-government organisations (NGOs), which sought to promote the moral case for protection from climate change and supported the European position for uniform cuts. Uniform emission targets were not only politically infeasible, but, because of different abatement costs in different countries, inefficient in economic terms and thus wasteful of resources (unless factors such as energy taxes were to be harmonised first). Many commentators have viewed the Montreal Protocol, with its precedent of international agreement in the face of a scientific consensus, as the model for FCCC; but whereas the ozone issue affected a few chemicals of marginal importance, for which some industrial interests made substitutes, climate change entails activities which are of central importance to the national interests of industrialised states. Climate science is also much more complex and much more uncertain, especially with regard to the effects of climate change. The negotiation of the Protocol showed clearly that differences in interests between parties must be recognised and negotiated, and that attempts to submerge them in moral injunctions would not suffice (Sprinz & Vahtoranta, 1994; Kellow, 1997).

Trading Emission Rights vs Carbon Taxes

Consideration of the political economy of the Kyoto Protocol leads us to consider the kind of policy instruments that might be adopted to mitigate greenhouse-gas emissions internationally.

Uniform percentage reductions using regulatory approaches are clearly inferior, especially since they are capable of producing counterproductive effects by creating perverse incentives (Maloney & Brady, 1988). A policy of percentage reductions of sulphur dioxide emissions in the US favoured the use of high sulphur coal, and was claimed to have produced worse outcomes than would have occurred in the absence of any policy. Kyoto reflects an awareness of this, especially since the absence of commitments by developing countries is likely to have simply resulted in carbon leakage. But such approaches sit well with the 'blame and shame' approach of the NGOs, which locks the problem into the North-South debate. Economic incentives, while usually more effective instruments, are not universally preferred. For reasons explained below, an emissions trading regime, as provided for in the Kyoto Protocol, is to be preferred to the main alternative of an international emissions tax; but the continuing opposition to either mechanism, largely reflecting an ethical objection to any permissive approach to the 'sin' of pollution, could result in difficulties being created in negotiations leading to the development of an emissions trading regime (see Goodin, 1992). The NGOs could well work to sabotage the highly complex negotiations which must now occur, by attempting to burden the regime with unworkable or unreasonable requirements. Care will be needed to avoid this.

Why is emissions trading to be preferred to taxes? A uniform carbon tax applied in all countries would achieve welfare-efficient abatement if the tax were set at the marginal damage costs of CO₂ emissions. But the exact nature and value of the physical damage remain unknown. Besides, if such taxes were to be collected domestically, they would create a compliance problem, since they could be partially

offset by governments reducing existing energy taxes, thus undermining the effectiveness of the international tax. If carbon taxes were to be collected internationally, this would imply a loss of sovereignty which would go beyond the level entailed in the FCCC. There is no precedent for a supranational agency collecting taxes. An additional problem is that international taxes, when combined with the double-standards provision of the FCCC exempting developing countries from binding commitments, could encourage carbon leakage, since taxes would suppress demand in Annex I nations, thus resulting in lower world prices for fossil fuels and encouraging increased consumption in non-Annex I nations.

Tradeable permits are regarded as preferable to taxes when the costs of abatement are known with greater certainty than the costs of potential damages and there is a significant probability of catastrophic damage (Pearce & Turner, 1990). These conditions certainly obtain with greenhouse-gas emissions. Once emission permits have been distributed, their value can reflect both developing views of the seriousness of the problem and the cost at which abatement can be achieved, and the market can reflect both changes in scientific knowledge and technological advances without governments having to readjust the level of taxes. If there are significant advances in photovoltaics, nuclear fusion, or CO₂ removal from power station emissions, permits will have a lesser value and this will be reflected in the cost of electricity from fossil fuels.

Taxes have the advantage of providing (at least potentially) less uncertainty over price, but at the cost of greater uncertainty over the quantity of emissions. They have some appeal to economists, but they are less likely to be favoured in decision processes driven by science and inevitably centred on atmospheric concentrations and thus quantitative emission limitations and reductions — as the Kyoto process was. Moreover, uncertainties over price under a trading regime can be addressed by futures trading.

The creation of a market in permits, including a futures market to guide longer-term infrastructure decisions, has considerable appeal to economists. Such a market 'should automatically clear at the global marginal cost of CO₂ control, thus eliminating the centrally determined estimates of such costs needed to impose an international tax' (Mabey et al., 1997:31). The use of such market instruments is preferred by economists as an alternative to heavy-handed 'regulation', but it should be remembered that they must themselves be underpinned by regulation. This is most obvious in the case of compliance issues in a market for permits, since some form of penalty must be set if nations emit more carbon than is covered by their permits. Since such penalties would have to be imposed by some international body, emissions trading raises sovereignty issues, just as taxes would.

Permit trading between nations would also give them flexibility in their own use of policy instruments to meet their targets: taxes, regulation, subsidies or domestic trading schemes. Such flexibility extends, of course, to the international level. Nations could choose whether or not to trade once the distribution of entitlements were decided, and could make their own decisions based on their assessment of abatement costs and other national circumstances.

The Kyoto Protocol allows international trading between firms; and while it does not make the establishment of a domestic emissions trading regime compulsory, it is highly likely that nations will decide to establish such systems as a means of integrating domestic climate change policy with the international system. The full ramifications of such developments will become evident only with time. Divisions will emerge between industrial sectors, most obviously between 'sink' sectors (such as forestry) and emitting sectors. It will take a considerable time for all these sectors to understand how their interests are affected. The proposal by McKibbin and Wilcoxon (1997) for national based emissions trading only in the absence of targets would have been much less problematic, but that is now not likely to be adopted unless Kyoto fails — as is possible.

There would appear to be insufficient time between now and the Fourth Conference of the Parties in November 1998 for the details of an international emission trading regime to be defined and designed, let alone negotiated. A likely outcome is a 'Buenos Aires Mandate', followed by another series of meetings of an ad hoc group to progress it. Yet international climate change policy appears headed in the right direction.

If entitlements are distributed initially much in line with existing uses, and reflect national determinations of abatement costs, their impact need not be too severe and industry will not oppose them as vigorously as they would taxes. Questions arise over such issues as entitlements for new industries, but there is no reason why they cannot be purchased from sink industries such as forestry or from those making energy-efficiency gains or other means of abatement. This is likely to affect the competitiveness of location in Australia only marginally for most industries, since energy costs are only one of several locational factors. Given that brownfields expansion in sectors such as aluminium smelting is likely to be cheaper than greenfields expansion elsewhere, and given that Australia still has substantial reserves of cheap coal, assigning property rights to carbon emission entitlements will not have the same impact on Australia's future economic prospects that a percentage reduction with no trading would have — while still creating incentives for emission reductions and sink creations.

An emissions trading regime could be responsive to the emerging science over both the extent of climate change and the distribution of its costs and benefits, whereas this would not be possible with carbon taxes, since one needs a good idea of the amount of the damage in order to set the rate of tax. While the rate of tax could be adjusted in the light of climate science, a tax could not be guaranteed to deliver the specified quantified reductions favoured by international negotiations.

An issue that has to be resolved is the incorporation of reductions in land clearing in Australia's allocation of permits, and how the gains resulting from reductions in clearing rates since 1990 should be distributed. A further issue is who should benefit from sink creation paid for under the Natural Heritage Trust Fund. These issues imply a need (presumably) to enforce covenants over land-based sinks to ensure that subsequent landholders continue to manage them in such a way that they continue to lock up carbon. The superiority of emissions trading makes it

worthwhile to resolve these problems, even though they are not likely to be resolved in time for the meeting in Buenos Aires.

Environmental Technology and Unintended Consequences

A note of caution should be sounded about the possible unintended environmental effects of emissions trading. Enthusiasts for different energy sources, whether inspired by technical or economic considerations, are prone to understate the associated drawbacks. In the early 1980s, the Tasmanian Hydro-electric Commission often claimed that (land use and wilderness values aside) hydro-electricity was non-polluting. This claim overlooked the temperature pollution which can kill wildlife when water is released from deep storages, the supersaturation with nitrogen which can result from releases from high spillways, and the heavy metals which can be mobilised from vegetation and geological formations. As well, the methane released from the creation of a hydro storage in some locations could have roughly the same effect on climate change as would the generation of an equivalent amount of energy by the burning of fossil fuels.

This principle extends to many of the technologies that are advocated so enthusiastically as being 'renewable'. The largest wind farm in the world, at Altamont in California, has a visual impact, makes noise, causes soil erosion and kills more birds every year than were killed by the Exxon Valdez, the oil tanker that foundered on the Alaskan coast in 1989. Solar thermal and photovoltaic arrays have similar impacts, and photovoltaic cell production gives rise to emissions of toxic arsenic, gallium and cadmium. The land requirements for central photovoltaic arrays are 2-4ha/MW of installed capacity, and solar thermal slightly more.¹ A 2000MW power station would thus require in the order of 5000ha of land, which would have to be purchased and would amount to a substantial 'footprint' in an important habitat. Such technologies should not necessarily be eschewed — many of the impacts noted above can be minimised with careful siting, for example — but their costs as well as their benefits should be calculated. In view of this, attempts at 'green energy' labelling which include the renewables listed above but exclude coal-bed methane (see, for example, SEDA, 1997) are open to question. Given that coal is likely to be extracted to some extent in Australia for a very long time, it makes sense to use a significant greenhouse gas to produce energy rather than to release it into the atmosphere.

Conclusion

The Kyoto Protocol has not been widely welcomed. Environmentalists in Australia tend to see it as letting Australia off lightly, while greenhouse sceptics reject it as imposing legally binding requirements to reduce emissions they see as unwarranted.

¹ See Bradley (1997). It should be noted that Bradley is an enthusiast for gas, but this underscores the need for the different interests on issues such as climate change to probe the weaknesses of different schools.

Especially because it does not include any binding commitments from developing countries (not even to slow growth in emissions), its ratification by the US Senate is highly problematic.

Realistically, Kyoto must be seen as the first step in a long process to create a set of 'insurance institutions'. Much detail in terms of compliance mechanisms and provisions for emissions trading is yet to be defined, and this is not likely to be completed at the next Conference of the Parties. But while Kyoto was but a first step, it inaugurated a journey in a promising direction. While some might argue for the superiority of taxes, the provision for emissions trading adopted in Kyoto appears better suited to both the problem in hand and the realities of international negotiation, although both raise important issues such as sovereignty.

The acceptance of differentiation was inevitable since Parties would commit only to what they considered equitable in the context of the circumstances of others. In the face of the European bubble, no responsible government is likely to have committed to a binding target which implied a greater burden for its citizens than was being accepted by the Europeans. If the special circumstances of Spain, Greece, and Sweden were accepted within the EU as grounds for allowing differentiated commitments, then why should those of Iceland, Norway and Australia be ignored? And if Germany and the UK could trade their windfall reductions within the EU, why not Russia within APEC? Not only was differentiation fair, it was realistically the only possible outcome.

Kyoto represents the triumph of interests over idealism in international negotiations. It is a modest success which remains vulnerable to both interests and ideals.

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Global Emissions Trading: A Post-Kyoto Proposal

Warwick J. McKibbin

AT a conference held in Kyoto, Japan, in December 1997, the Parties to the UN Framework Convention on Climate Change agreed to a Protocol to reduce global greenhouse emissions. Although heralded by many as a breakthrough in climate change policy, the Protocol is fundamentally flawed and in its current form will probably collapse if adopted. Its flaw is that the main focus is on achieving rigid 'targets and timetables' for emissions reductions at any cost rather than on substantial reductions in emissions at reasonable cost.

A good deal of uncertainty surrounds the costs and benefits of cutting greenhouse emissions; yet the Kyoto Protocol forces emissions back below 1990 levels without regard to the costs or benefits of doing so. Current evidence does not give clear support to a policy of holding emissions constant, let alone reducing them significantly. The costs and benefits of the Kyoto targets are not known with much precision; but most studies of costs of stabilisation arrive at estimates that are higher than the highest estimates of benefits. Moreover, it would be necessary to start to pay these costs now in order to avert damages far in the future. Given these considerations, it is difficult to believe that the United States Senate would ratify a treaty based on reducing greenhouse gas emissions below 1990 levels. There is, however, enough evidence to make a clear case for taking steps to slow the growth of greenhouse emissions. A better policy would focus on this more modest goal.

The move away from uniform targets for every country occurred at the Kyoto meeting because they were correctly seen to be very inefficient and politically infeasible. A crucial, but mostly ignored, issue is that any fixed targets, even differentiated targets, are likely to be inefficient because their costs over the long period of time being discussed are not known.¹

The post-Kyoto negotiations are now focused on attempting to make the problematic rigid target approach work by using economic instruments to minimise the efficiency losses from the agreement. In principle, these instruments look promising; indeed, the Kyoto Protocol explicitly incorporates the idea of using global

¹ See McKibbin and Wilcoxon (1997a) and Kopp et al. (1997) for arguments about the difference between price and quantity caps under uncertainty.

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emission trading permits or umbrella groupings of permit traders as a way to implement the Protocol. Unfortunately, while the advantages of a permit trading system at the domestic level is well established through other emissions trading schemes (such as the US sulphur dioxide scheme), and the global schemes seem theoretically sound, few researchers have understood the adjustment problems involved in implementing such a proposal.² McKibbin and Wilcoxon (1997a, b) point out that a global emission permit trading system with caps on the number of permits (that is to say, an explicit and binding emission target) is a dangerous path to take because, under some scenarios for the evolution of the global economy, the Protocol may be abandoned because of economic and political problems outlined below. In an attempt to overcome the potential flaws in this scheme, we have proposed an alternative policy that would achieve real greenhouse gas reductions without the potentially disruptive political and economic problems of a global permit trading scheme that is built around fixed targets and timetables. This is a globally coordinated system of domestically implemented permit trading schemes with a fixed common permit price across all countries. Richard Cooper (1996) has called this an 'agreed actions' rather than an 'agreed targets' approach. The idea is to produce a system that falls between the extremes of rigid targets and inaction on climate change policy.³

How Do Permit Systems Work?

The basic idea behind a tradeable permit system is simple. Any firm emitting carbon dioxide (or the carbon dioxide equivalent of a broader range of gases) would be required to own permits equal to the amount of carbon it produces. For example, a firm emitting 100 tons of carbon would have to own 100 permits. The permits would be allocated among countries by treaty, and each government would decide how to distribute its permits domestically. Once distributed, the permits could be bought and sold without restriction on a world market. It would be illegal to burn fossil fuels without having purchased a permit, and it would be up to each government to enforce the treaty within its own borders.

Permit systems have three key features as a method of pollution control. First, they provide a firm upper bound on emissions. This feature makes permits attractive to those who believe that decisive action needs to be taken on climate change.

Second, because the permits can be traded, pollution abatement will occur at the minimum possible cost to the economy. Firms that can clean up cheaply will carry out the abatement: they will be able to make a profit by cutting their emis-

² See Hartley (1997) and Cornwall et al. (1997) for an overview of permit trading and its desirable properties. Like most studies, these papers ignore the international economic adjustment problems.

³ In addition to the proposal forming the basis of this article, Anderson and McKibbin (1997) estimate that a significant reduction in greenhouse gas emissions can be achieved at low cost by removing existing distortions in world coal markets. Such a policy should precede the implementation of the proposal discussed here.

sions and selling their surplus permits. Firms that find it very expensive to reduce emissions will buy permits instead.

Third, permits will ensure that the marginal cost of reducing carbon emissions is the same in all countries that participate in the scheme. In other words it would cost the same to remove a unit of carbon from each country participating, so no lower-cost options will remain.

If a global permit system were implemented following the Kyoto Protocol, countries would presumably be allocated an initial stock of permits equal to their targets. For example, Australia would receive permits equal to 108 per cent of 1990 emissions whereas the United States would receive permits equal to 93 per cent. These would be allocated within countries, and firms could trade with one another in a global market. Given that the marginal abatement costs (the incremental cost of reducing emissions) are estimated to differ across countries,⁴ the permit price would be somewhere between the lowest and the highest marginal abatement costs.

A global permit trading scheme appears to be a very attractive way to implement the Kyoto Protocol. It performs well when run through global models under multiple scenarios, and clearly minimises abatement costs in the longer run. However, a number of potential problems can be identified that are related to the nature of the adjustment path rather than the long run.

What Could Go Wrong in Practice?

Permit systems have worked well when used to control domestic environmental problems. The best-known example is the sulphur emissions trading scheme introduced by the 1990 amendments to the United States Clean Air Act. It has been a tremendous success: electric utilities, the principal industry affected by the programme, have been able to reduce the cost of controlling sulphur emissions to one-tenth of the minimum cost projected when the act was adopted. For controlling carbon dioxide emissions in an international context, however, several practical problems arise that ensure that a treaty based on an international permit trading scheme would be very difficult to ratify or implement in the US.

A fundamental problem with a conventional global permit system with a fixed supply of permits is that it could generate large transfers of wealth between countries. This is not likely to be a problem for a system including only the developed Annex I countries. But it becomes a more serious potential issue when the system is expanded to include the major developing countries. Supporters of a permit system regard the wealth-transfer properties of the permit scheme as an advantage because it would allow developed countries to compensate developing countries for reducing their emissions. This would be a significant political problem for the US Congress. But, more important, it could put enormous stress on the world trade system. The balance of trade for a developed country importing permits would deteriorate substantially. This would lead to substantial volatility in exchange rates and distortions in the world trade system. Equally serious problems would be cre-

⁴ See ABARE (1997) and McKibbin and Wilcoxon (1997c).

ated for developing countries. Massive exports of permits would lead to exchange rate appreciation and a decline or collapse in exports other than permits.

Another problem is that the permit revenue for developing countries comes with strings attached: much of it would have to be invested in improved energy technology in order to reduce emissions and free up the permits in the first place. This is unlikely to be an ideal strategy for long-term economic development and would make the policy unattractive to developing countries.

In fact, developing countries have been so unenthusiastic about the policy that the Kyoto meeting produced support for an umbrella group to trade emission permits (including Australia, New Zealand, Canada, Japan, Russia, Ukraine and the US). However, this is a compromise that significantly weakens the main reason for having internationally tradeable permits: the potential gain from trade in emissions rights between industrialised and developing countries. Permit trading would do little to lower abatement costs when the participating countries have fairly similar marginal abatement costs. Moreover, this umbrella system may not even reduce emissions, because Russia and the Ukraine are well below their 1990 emission levels and would be able to sell their unused permits within the umbrella group. In that case, the permit system would really amount to nothing more than an elaborate accounting mechanism for counting increases in emissions in countries like the US against the 1990 allocation for Russia; there would be little or no overall reduction. But under a plausible alternative scenario in which Russia grows strongly between now and 2008, the demand for permits within Russia would increase, sharply driving up the umbrella price of permits. This could add an ironic twist to an international permit policy: if Russia were to grow quickly, the US could soon become the developed world's low-cost emissions abater. In that case, the US would be a net seller of permits, and the rest of the industrial world would end up paying it to reduce its emissions. Under the scenario outlined, this is exactly the outcome that efficiency would dictate; but it would be politically fatal to the Kyoto Protocol in the US. Most important, serious greenhouse abatement will only occur in a system that includes developing countries. Whatever emerges from post-Kyoto negotiations should have this as the paramount objective.

Another problem with the Kyoto Protocol and any conventional permit trading system under a fixed target is that no individual government would have any incentive to police the agreement. It is easy to see why this is so: monitoring polluters is expensive, and punishing violators imposes costs on domestic residents in exchange for benefits that will accrue largely to foreigners. Governments would be strongly tempted to ignore firms exceeding their emissions permits. For the treaty to be viable, however, each participating country would need to be confident that all of the other participants were enforcing it. It is clear that such a system would require an elaborate and expensive international mechanism for monitoring and enforcement.

A final problem is that the supply of permits would be from each country participating and hence any country that cheats on the system will potentially undermine the value of permits for the entire system. Once the value of permits becomes highly uncertain, the system is vulnerable to collapse. To see this, consider the case

of government bonds issued by different countries. These are essentially the same instruments, but each is priced differently in world markets purely because government bonds are issued by different governments. Thus, different sovereign risks are priced into government bonds from different countries precisely because there are different degrees of uncertainty about the ability of governments to honour these assets. Now consider the potential disruption to global bond markets if all countries were able to issue exactly the same bond that was redeemable in any other country. The system would be vulnerable to collapse if one country behaved inappropriately and undermined the value of all government debts. Thus, a world permit system with a fixed supply of permits and a variable permit price would be very difficult to hold together because it would require enforcement procedures and a rule of law that currently do not exist at the global level.

All in all, an international permit system aimed at a fixed target for greenhouse emissions is unlikely to be politically viable in developed countries, could distort or compromise the world trade system, would be unattractive to developing countries, and would be difficult to monitor and enforce. It is an impractical policy focused on achieving an unrealistic goal.

An Alternative to Fixed Targets

McKibbin and Wilcoxon (1997a, b) have advocated a policy that gets around the potential problems of a global permit trading scheme discussed above. This a system of internationally coordinated but domestically administered permit trading systems with a fixed price in each system. In many ways our approach seems like a small movement away from the global permit scheme with a fixed quantity of permits, which retains many of the advantages but removes crucial problems. Despite the apparent similarities, our approach is philosophically far removed from the degree of centralisation implicit in a global permit scheme, which has very different political implications.⁵ Our proposal, as originally designed, is an internationally coordinated system of national permits and emissions fees for carbon dioxide, although it could easily be extended to incorporate the six greenhouse gases identified in the Kyoto Protocol.⁶ Under this system, all emitters would be required to own permits equal to their total emissions of these gases.

There would be two stages of permit distribution. In the first stage, countries would be allowed to distribute a specified number of permits to their domestic emitters in any way they liked, including handing them out for free. To minimise administrative costs, the permits would be based on the emission of carbon at the

⁵ Our proposal has become known as the McKibbin-Wilcoxon Proposal in the international debate; but, for whatever reason, has been called the McKibbin Tax in the Australian debate: inappropriately in my view, because most of the revenue from the purchase of permits is a transfer within industry not between industry and the government. Only a small part of additional permits sales accrues to government.

⁶ Carbon dioxide, methane, nitrous oxide, hydrofluorocarbons, perfluorocarbons and sulphur hexafluoride.

original source of energy such as the coal mine and oil and gas extraction industries. Although this is where the permit is required, these producers do not bear the full burden of the cost, since this will be passed through the production and consumption chains with some portion of the permit price being reflected in the final price to end users of carbon-intensive products.

The key to our system is that, rather than allow permit trading to set the market price, the price of permits will be fixed by international agreement. The market trading will then determine where abatement occurs, but at the fixed price. We propose a fixed permit price of US\$10 a ton of carbon, because this is well below the price that most models estimate a stabilising permit price would be. So at the fixed price, there will be an excess demand for permits. Once a firm receives an initial allocation of permits from its government, the firm will have to decide whether to buy additional permits, sell some of its allocation, or stay with exactly the number it was given. If it does not buy or sell permits, it can continue with its existing practices at no additional cost (although there is a significant opportunity cost from not selling permits). If it needs to increase its carbon-emitting activities, however, it will have to buy additional permits at a price of US\$10 a ton, giving it a clear incentive to avoid increases in emissions. At the same time, if the firm could reduce its emissions, the permit system would give it a strong incentive to do so: avoided emissions could be sold on the permit market at a price of \$10 a ton. For example, if an electric utility could shift some of its load from coal to natural gas for a cost of \$6 a ton of carbon, it could emit less carbon and make a profit of \$4 a ton by selling its excess permits. Indeed, many firms have claimed they are willing to undertake low-cost carbon abatement. The permit system we propose will reward firms for these endeavours. The more effort a firm puts into reducing carbon emitting activities at low cost, the higher its profits will be.

After these permits are allocated within each country an unlimited number of additional permits could be purchased from each government by domestically located emitters at a stipulated international price of US\$10 a ton. Thus, the price is held by governments being willing to sell additional permits to satisfy the excess demand emerging from permit trading among domestically located firms. Because the total number of permits can rise if abatement turns out to be expensive, the policy has safeguards that would limit the economic damage that the policy could inflict. Yet we have chosen a price which most studies estimate will generate a demand for permits in excess of the initial allocation (this could be based on 1990 emissions or the Kyoto targets but would be negotiated).

Since the policy does not focus on achieving a specified target at any cost (indeed the cost is known with certainty), such a system would be far more likely to be ratified, and by more countries. This policy is not simply a uniform carbon tax, as it is often portrayed. Only marginal emissions above the target are subject to a direct charge (the price of permits); but most of this is a transfer within industry rather than between industry and government. Indeed, existing emitters are implicitly given subsidies to change their behaviour because the opportunity cost of continuing with their activities is the permit price. If firms do nothing, they are not

subject to any direct cost increase but are awarded profit in proportion to their success at reducing emissions.

Although at first sight it appears that existing industry and new industry are treated differently, this is not the case. Existing emitters would experience a decline in the value of capital. They will have to change their capital stock over time. These existing emitters receive lump-sum compensation for the change in the value of existing capital stock that the permit system would cause. This compensation is proportional to the amount of abatement achieved. A unit of carbon emitted will cost both new and existing firms the same because new firms must buy the permit, but existing firms must decide whether to keep the permit at the cost of the permit price or to reduce emissions. Either way, the permit price will affect the costs of the two types of firms in exactly the same way.

In principle, this system could also deal with the issue of sinks of greenhouse gases by allowing producers of sinks (land-use changes, tree planting and so forth) to be awarded permits for their activities that they can then sell into the permit market. There are serious issues of measurement that need to be overcome to ensure that the system is not debased; but in principle a generalised McKibbin-Wilcoxon system would be possible and would be more feasible in each domestic system than at the global system because of differential measurement of sinks across countries (though it is not considered in this article).

The McKibbin-Wilcoxon proposal as extended here has a number of advantages. First, the same price will be charged for each new permit in each country as well as for any permits that are traded in domestic permit markets. Thus, the marginal cost of reducing carbon emissions will be equalised within and across all countries that participate. This makes the system efficient because the cheapest emissions reductions will be undertaken first. Environmentalists and engineers often argue that many low-cost options are available for reducing energy demand. If so, these low-cost options will be exploited under this policy, without needing to be specifically identified in advance by the government. On the household side, for example, the increase in energy prices will encourage households to demand more energy-efficient vehicles and appliances.

Second, the policy contains built-in mechanisms to encourage enforcement. Governments will have an incentive to monitor the system because they will be able to collect revenue from selling permits. Firms will have an incentive to monitor one another because any cheating by one firm would put its competitors at a disadvantage and would also affect the value of permits held by other firms.

Third, the system is flexible and decentralised. New countries can join by setting up their own permit systems and agreeing to charge the stipulated world price for additional permits.

Fourth, transfers associated with the permit system are largely between firms or between firms and households, rather than between the private sector and the government. The proposal also minimises transfers across borders, avoiding serious economic and political problems. Unlike the experience of the 1970s, increases in

energy prices under this policy would not lead to massive transfers of wealth between countries.

Fifth, the policy also could be revised easily as more information becomes available. After setting up the system and agreeing on the price of permits, participating countries could meet every five years to evaluate the extent to which carbon emissions have been abated as well as to re-evaluate the extent of climate change and its consequences. If it becomes clear that more action is required, the permit price could be raised. If climate change turns out to be less serious than it appears today, the permit price could be lowered. To minimise the costs of these price changes, future markets could be developed in permits so that risks are effectively shared.

Sixth, if any country decided to renege on its commitments, this would only mean emissions globally would be higher than otherwise, but the value of permits in other countries within the system would not be undermined and the system could hang together as countries leave and enter the system.

Overall, the advantage of the McKibbin-Wilcoxon proposal for a domestically managed, but internationally coordinated, permit and fee system over the targets and timetables approach of the Kyoto Protocol is simply that it is far more practical. It is more likely to be ratified by key countries because it limits the cost of compliance and does not require governments to commit themselves to achieving a given target at any cost. It is more likely to be acceptable to developing countries because it is not a Western-controlled centralised system. It is transparent to households and firms globally because it spells out exactly how the policy will work, rather than specifying the target and leaving the policy undefined. It is more credible than a targets and timetables policy because it is not so draconian that countries will be tempted to renege under extreme future scenarios, and because the revenue from selling additional permits will give governments an incentive to enforce the agreement over time. Existing industry is less likely to oppose it because compensation is built into the system. Moreover, because it contains a mechanism for limiting economic costs, the risk of setting ambitious emissions targets, which could significantly reduce economic growth if abatement proves to be expensive, is eliminated. This would remove the single most important obstacle to reaching a realistic international climate policy.

Most important, our system explicitly deals with the uncertain nature of the climate change problem and allows plenty of flexibility when new information emerges on the costs of abatement, changes in climate and new developments in climate science. It is also more likely to survive the political uncertainties of changing country commitments over time.

What Should Australia Do Now?

Australian policy-makers now face a dilemma. They have signed a Protocol which is subject to a great deal of uncertainty about ratification by key countries. A meaningful agreement hinges on how developing countries are included and this will become clearer in Argentina in November 1998 with the fourth meeting of the Conference of the Parties to the Framework Convention. If the Kyoto Protocol

does proceed, action will need to be initiated in Australia because, despite beliefs to the contrary, Australia has a good deal of abatement to be implemented by 2008. My research suggests that carbon dioxide emissions from fossil fuel use will reach 150 per cent of 1990 levels by 2010, using plausible assumptions (with a great deal of uncertainty around this number in both directions). Adding other sources of emissions complicates the actual emission calculation, and incorporating sinks further complicates the extent of adjustment required. Nonetheless, Australia's target of 108 per cent of 1990 levels by between 2008 and 2012 will potentially require significant policy changes.

If Australia is to participate in an international agreement like the Kyoto Protocol, action should start as soon as possible, but after the Protocol is ratified by the US. This is particularly important for industries that need to make long-term investment decisions. In the meantime, Australia should lobby the international community to move away from the fixed targets approach enshrined at Kyoto towards action based on permit trading with a fixed low price. The proposal for a fixed-price scheme set out here could be made consistent with the Framework Convention on Climate Change. There could be a clear statement that the goal of the policy is a reduction in emissions. To achieve this, every five years countries would meet to consider the success of the permit trading schemes in reducing global emissions and then negotiate a price for permits that would lead to convergence of emissions towards the stated goal. This learning by doing approach to international policies is a far more sensible way to proceed.

There is already considerable interest in the McKibbin-Wilcoxon proposal (or variations of it) at the international level, although most negotiators argue that it is currently infeasible to change direction so fundamentally in view of the current state of negotiations.

If the Kyoto Protocol is ratified by the US, and the world continues to use rigid targets, it would be sensible for Australia to start a domestic permit trading system. This would place it in a good position if and when an international permit trade system is implemented. There is, however, a serious problem that should be considered. For carbon emissions alone, we estimate that marginal abatement costs for Australia are high and certainly higher than for the US.⁷ Thus, the price of permits in an Australian domestic system would be expected to be much higher than the price in a system that included the US, which has low estimated marginal abatement costs, or even one that included Russia, which would bring a significant volume of essentially 'free' permits to the system. After all, if the prices of an Australian-only system and a wider group of countries were the same, a permit trading system would be unnecessary because there would be no gains from trade across national borders! So a permit system within Australia with a cap on permit quantities equal to the Kyoto emission targets could be a very bad idea in the near term because any subsequent participation in a multi-country system would most likely lead to a large fall in the permit price in the future. Why pay a high economic price in the short

⁷ See McKibbin and Wilcoxon (1997c) for some estimates.

term? If Australia is seriously going to reduce greenhouse emissions, an alternative approach would be to introduce a McKibbin-Wilcoxon system in Australia with a very low fixed permit price of, say, A\$5 a ton of carbon-equivalent emissions. Thus, the cost of abatement would be known and fixed for a period of several years. A low price with market-determined abatement would ensure less economic disruption than a market-determined price. The permit price could then be adjusted, either independently by Australia or as part of entering into a wider system with more countries.

Given the many uncertainties with the current state of negotiations, the international community may yet adopt the global system consistent with our proposal for a decentralised fixed-price permit trading system. It would be sensible to implement this in Australia sooner rather than later. Even if the international community continues to move towards a multi-country system with a fixed target for emissions, there is a strong case for implementing a fixed-price permit system in Australia in the short run. A domestic fixed-price system with a low initial price would minimise the costs to Australia during the transition from a domestic permit system to a global permit system.

Summary

The Kyoto Protocol is a bad outcome for global environmental policy. It has created a great deal of uncertainty about how and whether countries are going to achieve by 2008-12 the strict quantity targets that have been set. The international community had an opportunity to implement a credible instruments-based approach that would begin to reduce emissions at low cost wherever possible, in addition to giving flexibility to the time frame and burden-sharing arrangements. Policy-makers now have to turn to economic instruments within a target regime that has many potential risks.

For researchers of climate change and for negotiators and bureaucrats, Kyoto was a full-employment contract for many years to come. For the world economy, it has presented many crucial challenges. Our goal should be to make the system that develops as decentralised as possible and to ensure that Australia does not commit to a significant loss in economic well-being while waiting for the other key countries to participate. If greenhouse gas emission reductions are to be pursued — and this will need to start soon if Australia is serious about the Kyoto Protocol — one way forward is a domestic version of the McKibbin-Wilcoxon proposal outlined in this article. In this case, a tradeable permit system could be implemented within Australia but with a very low fixed price for permits. The initial allocation of permits could be the Kyoto target. The market would then be used to determine the extent of abatement at a known cost. This begins the greenhouse reduction process at the same time as keeping costs low until the outcome of a decade of future negotiations is realised.

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An Economic Analysis of New Zealand's Conservation Strategies

John L. Craig

A recent publication from the New Zealand Business Roundtable titled *Conservation Strategies for New Zealand*, and written for the Tasman Institute by Peter Hartley, an Australian-born economist at Rice University, Texas, briefly produced ripples of unease through New Zealand conservation circles. It was publicly dismissed by most conservation groups and Department of Conservation (DoC). Even Dr Nick Smith, the Minister of Conservation, condemned the report in the very week that his foreword to the government department's annual report noted that the conservation agenda included 'encouraging public participation in conservation' (DoC, 1997a).

Despite its importance, the debate about the publication appears to have stopped. No one has challenged the assertion by DoC senior managers 'that while economics has much to offer conservation ... this report ... has nothing positive to contribute' (DoC, 1997b). Is this the case? An analysis of conservation in New Zealand, of the contents of the book and of the reaction to it demonstrates the difficulties and conflicts that hinder effective conservation.

Conservation in New Zealand

Like many other parts of the world, New Zealand is continuing to lose biodiversity (MFE, 1997), has no biodiversity or sustainability strategy and little knowledge of natural capital, and lacks the accountability measures to ensure that it could achieve these goals if it had them. As with all island nations, biodiversity loss and degradation in New Zealand are more rapid than on larger land masses, and so require prompt and flexible management responses. Superficially, the New Zealand government can claim to have shown leadership on a range of issues; one of the most striking is the reservation (protection) of more than 30 per cent of the country's land area for conservation. But most agencies and the general public fail to appreciate that this measure is 'greenwash', in that it ignores the continuing decline in biodiversity across more than 95 per cent of this public conservation estate.

DoC is a government agency charged under the Conservation Act 1987 with 'the preservation and protection of natural and historic resources for the purposes of maintaining their intrinsic values, providing for their appreciation and recrea-

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tional enjoyment by the public and safeguarding the options of future generations'. Since its formation in 1987, its budget has been gradually declining, though it has been recently supplemented for tagged projects such as possum control and visitor safety. Its many deficiencies are usually attributed to inadequate funding. Regular calls by conservation non-governments organisations (NGOs) for additional government finance have been largely ineffective.

Since the fiscal crises of the 1980s, New Zealand has undertaken reforms that aim to reduce the role of government and increase the responsibilities of communities, agencies and private individuals. Conservation remains one of the few areas where no split has been introduced between the funders of government services and the agencies that supply them.

DoC was formed by an amalgamation of staff from sections of previous government departments including those responsible for national parks and reserves (Lands & Survey), native protection and former production forests (Forest Service) and large animal biodiversity (Wildlife Service). Each group brought a pre-existing mentality into the new organisation, whose overall approach was to separate the protection aspects of the old departments from the exploitative aspects (land development, extraction forestry and game control). The new department resolved the uneasy alliance of resource extraction and destruction with protection, but enjoyed only a limited capacity to raise money. The established mindset viewed people as the problem rather than the solution, and certainly not as customers. A strong culture emerged of lock-up protection with command and control management.

DoC has often examined its performance and attempted to redefine and enhance its role. For example, in 1992 it began to ask staff and associates what they wanted and what they thought was wrong. Maori wanted an active or sustainable approach to conservation rather than a passive lock-up approach. Associates (NGOs, councils, and government departments) had a 'poor' image of DoC, seeing it as 'overprotective ... driven by the certainty that it was always right ... bureaucratic, impractical and out of touch with reality' (DoC, 1992:7). Neighbours of the public conservation estate observed that DoC advocated 'protection' on private land while neglecting nearby parts of the conservation estate. The DoC management team argued that 'efficiency and accountability are essential but these are not always appropriate as core criteria' (DoC, 1992:5). The result was a restructuring (one of many) aimed at enhancing DoC's focus on protection of biodiversity and ecosystem processes along with a commitment to share responsibilities with a wide range of organisations, groups and individuals. Yet this apparently bold and self-searching initiative appears to have resulted in little change.

Early in 1994, Anne Stewart and I pointed out that DoC's annual reports appeared to dwell on actions rather than outcomes, which made it difficult to calculate conservation benefits. We argued that conservation benefited from a business approach and that emphasising the legislative requirement of actions for 'intrinsic values and for future generations' minimised accountability since the chosen customers had no voice (Craig & Stewart, 1994:165). We also stressed that current actions were not even maintaining existence values, since protection was implemented

largely through benign neglect. Our views were strongly influenced by a nationwide public survey that was published subsequently (Craig et al., 1995).

The eradication of kiore in 1993 from Tiritiri Matangi Island brought me into direct contact with the coercive aspects of DoC's conservation management, a factor consistently raised by Maori (see Taiepa et al., 1997). The island had been restored through replanting and reintroduction of rare fauna by massive community efforts initiated long before the establishment of DoC. Even though several Maori communities had requested a moratorium on kiore eradications (Roberts, 1995), DoC urged Supporters of Tiritiri to provide finance for an aerial drop of poison. When confronted in a meeting with the request that tunnels be used rather than an aerial drop in order to reduce incidental kills of rare birds and to allow long-term research programmes to continue, the DoC officials argued for net conservation benefit. For them, short-term kills of some highly threatened and some common species would not threaten long-term viability and would provide major conservation benefits. They dismissed as irrelevant research programmes on the island, which is classified as a scientific reserve. After threatening to 'close the island to the public' and 'to prevent all future translocations of animals' if resistance continued, the DoC officials got their way. Kiore were eradicated, the predicted loss of birds occurred (including the near-eradication of one species), and tens of thousands of dollars invested in independently financed conservation science were wasted. While the long-term result will be beneficial, the short-term result was unnecessarily destructive.

The 1995 tragedy at Cave Creek, where the collapse of a DoC-made viewing platform killed 14 people, profoundly influenced the approach of DoC, which immediately became preoccupied with responsibility and customer safety. The costs of this change of priorities further stretched a declining budget. Hampered by a parliament directive that free access meant free use, DoC was unable to recoup the additional costs of structure safety. Against the general trend towards user charges and closer targeting of welfare, taxpayers are in effect subsidising international tourists and local users predominantly from higher income brackets.

In 1997 New Zealand's first comprehensive report on the state of the environment appeared (MfE, 1997). It highlights the appalling state of the country's biodiversity and the continuing decline in both 'protected and unprotected' areas. Introduced herbivores, especially possum, goats and deer, are destroying the structure of forests and other ecosystems; while introduced predatory mammals, especially mustelids, ship rats and feral cats, are destroying much of the wildlife. In its recently published five-year plan, DoC (1998) reports that it has programmes in place to control sustainably possum and goats on approximately 15 per cent of the public conservation estate, which it hopes to increase to 25 per cent by 2000. The remaining area of more than 5m hectares of at-risk ecosystems is left to decline further, while virtually the whole estate is without protection from mammalian predators. These predators are wiping out birds and insects that are the main pollinators and seed dispersers, thus threatening New Zealand's forests and New Zealanders' ability

to experience functioning native ecosystems with most native species in more than relic densities.

Like much of the world until the late 1980s, New Zealand's approach to evaluating conservation relative to other activities relied on special value judgments rather than a mix of values, including economic ones. Consequently, the debate is predominantly political (three major conservation NGOs maintain head offices in Wellington, the political capital). The inevitable result, as Costanza et al. (1997:253) stress, is that 'because ecosystem goods and services are not fully captured in quantified terms comparable to economic services and manufactured capital, they are often given too little weight in policy decisions. This neglect may ultimately compromise the sustainability of humans in the biosphere'.

Peter Hartley's Contribution

Peter Hartley's book provides the first economic analysis of conservation strategies in New Zealand. As such, it could be seen as an extremely valuable aid to the Minister's objective of 'advancing the view that conservation is an investment' (DoC, 1997a:5). But it is important to realise at the outset that the book is not a complete or even a balanced analysis. The research was undertaken without any official co-operation from DoC. Hartley responds to the defensive reaction by DoC officials to his project by observing that 'DoC is a public organisation, not a secret one ... therefore, DoC has to be accountable to the people of New Zealand for its actions' (1997:27). The greatest strength of the book is its remarkable breadth. It clearly establishes many of the dimensions of the much-needed debate on conservation in New Zealand.

Hartley bases his evaluation on a selection of published documents from DoC (although he failed to reference many important policy documents such as the Conservation Management Strategies), and personal discussions and impressions received while travelling throughout the country visiting both the public conservation estate and the few private conservation enterprises. He examines the issues of legislation, structure and efficiency of government conservation; the possible role of greater non-government participation in conservation, including the role of markets (the ability of customers to dictate priorities through a willingness to pay directly); and ways to enhance conservation objectives on private land. He also examines Maori development and issues of historic heritage management. He only superficially addresses the multitude of externalities that allow parts of the business sector (especially farming, fishing and forestry) to avoid conservation (and sustainability) activities.

History and context. Chapter 1 covers the state of the New Zealand environment and the history of the public conservation estate and government reforms that led to the formation of DoC. Hartley then provides an overview of environmental management structures and the functions of DoC, public perceptions of DoC, and the importance of the Treaty of Waitangi. He comments on the overwhelmingly negative reception he received as a representative of business from most individuals and

groups associated with conservation. (Nowhere does he consider the current difficult relationship between the conservation movement and business in New Zealand.)

Resource allocation. Chapter 2 deals with markets, politics and voluntary activity. It sets out the broad dimensions of the current debate of government reform. Conservation, like many environmental issues, involves publicly owned resources the costs of use and abuse of which are hidden under the guise of being everyone's birthright. Contrasting the fate of moa and fishing with that of owned agricultural stock, Hartley points to the advantages of property rights in which privileges and responsibilities are clearly defined. He also contrasts market power (where individuals can pay for resources or services) with political power (where politically acceptable groups influence but where governments decide and provide, as is current in conservation). Some markets are inefficient because controlling access is difficult and free riding is possible; air and water pollution are salient examples of such inefficiency. The current lack of markets precludes informed discussion.

Hartley notes the considerable contribution of voluntary activity in conservation, even though it is sometimes subjected to bureaucratic obstruction. He concludes that community management of initiatives such as Tiritiri Island can enhance conservation outcomes at less cost to government. The lack of references to the considerable effort that some DoC staff are putting into fostering voluntary conservation in New Zealand probably stems from communication barriers erected by DoC senior management.

Competing uses for natural resources. Chapter 3 analyses the difficult wording of conservation legislation. The idea of 'intrinsic value' is problematic and self-contradictory; the law needs to be reworded so as to refer to a measurable value (examples of which are suggested). Quotations from DoC and non-DoC writers on conservation management reveal the contrast between the former's internally focused criteria and the latter's clearly articulated and customer-focused objectives that allow effective targeting of conservation resources. Removing references to 'intrinsic value' from the Conservation Act and placing the DoC-administered public conservation estate under the strictures of the Resource Management Act would greatly enhance conservation. This signals the importance of the philosophical debate about whether conservation is better promoted through protection (as under the Conservation Act) or through sustainable use (as under the Resource Management Act).

The inefficiency of political decision-making in conservation is illustrated with the example of Kaimanawa horses and contrasted with the example of efficient private high-country conservation where sheep threaten tussock ecosystems. In both situations, control of a grazer enhanced survival of native plant communities but politics dominated where a government agency was involved. Additional topics include maintaining conservation values through multiple use, integration of conservation with other economic goals, minimising cost by using local knowledge

(especially of Maori), and ensuring continuing management rather than lock-up neglect.

Achieving conservation goals. Hartley argues in Chapter 4 that all resource allocation decisions should take into account not only relevant environmental costs and benefits but also the costs and benefits of alternative uses of conservation land. Conservation of natural resources, to be achieved, needs to be integrated into economic decision-making. Given that there is no asset valuation of the public conservation estate that includes biodiversity, use, heritage and economic values used by groups such as Parks Victoria, Auckland Regional Council and New Plymouth District Council, Hartley's demand for accountable resource allocations among reserves is timely. No private organisation could survive with such a limited understanding of its assets or monitoring systems.

Hartley observes that DoC gives the protection of intrinsic values a higher priority than customer satisfaction. Since no objectives are declared and no cost-benefit analyses are undertaken, coherent policy-making is impossible. Hartley argues for consideration of net conservation benefit rather than simplistic justifications based on absolute rules determined by the values of government officials. The use of concessions and contract services suggests a largely ad hoc approach that focuses more on minimising risk or 'maximising revenue' (DoC, 1998:56) than on maximising conservation benefit. The estimated NZ\$44m spent annually on subsidising visitor services should be reduced.

Hartley questions DoC's ready acceptance of parliament's insistence that legislation requiring free access to areas managed by DoC means that they must be free to users. There is considerable debate on efficient allocation of visitor facilities and the value of obtaining customer profiles at the time of paying, a common practice in US parks. The currently inadequate information on customers and their needs is a likely cause of untargeted and often inefficient and inappropriate service provision. Hartley argues for charging users of the public conservation estate and for large fines for trespass, but suggests ways of charging New Zealand taxpayers and regular users less than tourists.

Hartley acknowledges that some people appreciate nature indirectly (that is, without ever visiting it), and that this justifies some public subsidy; but it does not justify monopolistic public supply of conservation value or providing it free to direct consumers of it.

The book refers to some examples of the greater conservation benefits that flow from ownership of, and strictly controlled markets in, wildlife than from trade bans that lead to black markets. However, it does not broach the logically related issue of customary harvest by Maori and the farming of native rather than introduced species: a seemingly contentious topic that requires wider debate. It similarly does not mention that DoC issue permits for killing animals that others would pay to keep in captivity if DoC allowed them to.

Private conservation. Chapter 5 covers the benefits of private as opposed to government provision of conservation, and outlines three successful examples of privately run ecotourism ventures with conservation benefits (Ngai Tahu Whalewatching, Yellow-eyed Penguin Trust, and Wainui Conservation Reserve). Earth Sanctuaries in Australia is discussed at length. These studies lead to the strong conclusion that NGOs can produce conservation values viably, but their operations are frequently frustrated by government competition and bureaucracy.

Hartley argues that taxpayer subsidy of government conservation deters private investment in conservation services. He concludes that some form of private ownership, or at least private management, should be considered where government land is primarily used for tourism and recreation, has local volunteer groups dedicated to its conservation, is most suitable for multiple land use or is primarily of interest to Maori.

Net conservation trades. Chapter 6 considers issues of multiple land use, sequential land use (such as mining followed by restoration), and offsets (where potential users of conservation land either purchase higher-value conservation land or provide finance that allows management to provide greater conservation outcomes from the area). Cases are cited of conservation groups unsuccessfully fighting for absolute conservation gains when compromise would have provided considerable benefits. Hartley concludes that the current situation in New Zealand where compensation for conservation activities on private land does not occur and where activities on the public conservation estate do not have to be justified in economic terms greatly reduces conservation outcomes everywhere.

The structure and performance of DoC. Quoting published evaluations of government reforms and the performance of DoC, Hartley stresses in Chapter 7 the inefficiencies of a department which, as one attendee of the launch of the book said, 'can act as both poacher and game keeper'. Furthermore, its multitude of functions — policy, advocacy, service provision, management of natural and historic resources — means that the provision of quality in one area often compromises quality in another. Arguing that conservation is predominantly a local issue, Hartley advocates a complete restructuring of DoC. Policy and advocacy should be split from service provision, and historic and natural resource management should be separated. Moreover, private conservation providers should be able to compete for government conservation funds. Reforms should focus on outcomes, including customer services, rather than functions, and so reflect the current internal structure of DoC (DoC, 1993).

All public conservation lands should be reclassified according to simpler and international criteria such as those of the International Union for the Conservation of Nature (IUCN). Moreover, there should be a capital charge on all public lands (returned to DoC) to encourage evaluation of alternative uses, and the sale of land with minimal conservation values. Suggestions for performance criteria and benchmarking are offered and compared with current reporting procedures. The

suggested changes are supported with little detail, but are in accordance with government restructuring elsewhere.

Maori development and conservation. The long-term disadvantaged status of Maori is outlined in Chapter 8, and issues of welfare and anti-discrimination are discussed in an international context. Noting the failure of external assistance through welfare and anti-discrimination legislation, Hartley argues, in line with current government thinking, that an economic base under Maori control should be considered. A conservation estate could provide an opportunity to establish a network of Maori property rights and, in accordance with Maori calls (see for example Taiepa et al., 1997), a true Treaty of Waitangi partnership as required in law. Circumstances would determine whether management was undertaken solely by Maori or in partnership with other service providers (such as DoC, universities, or Crown Research Institutes). As Hartley (1997:460) concludes, 'outright Maori ownership of conservation assets — with appropriate regulation — represents a far more equal relationship than the set of (revocable) promises by the Department of Conservation to "do the right thing" by Maori concerns'. At the time of writing, a Maori group is camping on DoC-managed land at Lake Waikarimoana protesting against alleged inadequacies in conservation management. In view of the initiatives in co-management with indigenous people undertaken in Australia and Canada, New Zealand clearly lags in this area.

Historic and cultural heritage. Hartley concludes that public ownership is not necessary for heritage preservation. Indeed, removal of the current disincentives for heritage protection would be part of a useful strategy.

Reactions to the Book

Reactions to the book were swift and largely predictable. In a press release issued on 18 December 1997, the Minister of Conservation 'rejected' the report, claiming it was 'based on greed and exploitation'. He claimed that 'charging for access ... would deprive thousands of New Zealanders of their birthright ... free public access is a core concept ... and is here to stay'. He announced that he would soon 'launch DoC's new business plan that would deliver more for conservation than the purist ideology of the Business Roundtable'. Additional comments about the privatisation of named locations and species (which are not mentioned in the book) and the subsequent release of the five-year plan suggest that the comment was ill-informed or meant to misinform.

DoC briefed its minister, its senior managers and 'interested stakeholder groups' on the contents of the book before its release. The brief (DoC, 1997b) contained the more contentious issues and took liberties in providing new and extreme examples. None of the rationale or justification for Hartley's recommendations was cited. Conservation groups, such as Forest & Bird and Environmental & Conservation Organisations, immediately went to press without reading the book, condemning suggestions such as entry fees and large fines for trespass, even though,

as Roger Kerr (1998) points out, these same groups made no comment when DoC introduced large fines for using DoC huts without paying associated fees.

The ministerial brief further argues that the Resource Management Act and the Conservation Act are 'not resource allocation mechanisms' as claimed in the book, but are there 'to ensure that the land is managed appropriately in terms of the use to which it has been allocated, with appropriate public involvement, cost recovery, etc.'. Suggesting that income from cost recovery, determining where and how often pest control is implemented, the issues of whether visitor services are provided and which types, whether concessions are allowed, how money is distributed among parks, and other such decisions made by conservation managers are not about resource allocation confirms Hartley's thesis that current conservation policy-makers believe they stand outside normal economic decision-making.

The briefing claims that the discussion on 'intrinsic values' is irrelevant because DoC interprets these to mean 'existence values'. (Prior communication of this might have softened Hartley's criticism and helped others working in conservation.) It further argues that accountability is unrelated to the precise wording of the Conservation Act as there are numerous other documents that provide a more concrete basis for decision-making and accountability. It is true that many documents detail conservation management approaches. Yet neither of these claims withstands scrutiny. For example, if decision-making is related to 'existence values', then the current pest-control programmes suggest that the existence values of native ecosystems are of little consequence. With less than 25 per cent of native ecosystems being protected, currently or prospectively, from the three major herbivores, and less than 5 per cent with adequate predator control, existence values must be declining over most of the estate. Yet few would accept that the role of DoC is to manage the decline of the public conservation estate.

The claim that accountability and decision processes are adequate must also be questioned in light of the December 1997 report of parliament's Transport and Environment Select Committee (New Zealand Parliament, 1997). This report was based on information from the Audit Office and the Parliamentary Commissioner for the Environment, both of which noted poor reporting of activities. The report records that the Audit Office noted that information-reporting systems were inadequate and that there was little evidence of self-review or peer review. The Commissioner for the Environment is recorded as saying that DoC's reports did not provide a clear picture of the department's achievements and gave very little sense of the actual results for conservation. Nor did annual reports 'set out the quality, effectiveness or relevance of the department's outputs'. Moreover, 'the annual report contained little precision about the methods by which the department assessed and monitored its activities and gave no clear sense of the medium and longer term directions for the department's contribution to conservation management in New Zealand' (New Zealand Parliament, 1997). It appears that the concerns raised earlier by Craig and Stewart (1994) have not been addressed.

The ministerial brief further dismisses the shift in emphasis that Hartley advocates from intrinsic value to public appreciation. The fact that few people 'enjoy'

small and ugly invertebrates is used to argue that the existing approach is best. DoC's five-year business plan (DoC, 1998) offers a greater acknowledgment of the importance of peoples' values and provides some more specific reporting targets. However, it still lacks a clear focus, did not receive appropriate public input and retains imprecise wording (such as 'when appropriate') that allows management control always to override stakeholder challenges and retain an internal management focus. Moreover, the comment that the public does not appreciate invertebrates is countered by World Wildlife Fund's nature-trail initiative and the impending restoration of a private island.

Stephens and Lawless (forthcoming) argue that DoC's use of public values to influence funding allocations will result in the type of conservation that the public wants being subsidised by the types they do not. Moreover, they argue that as the public can already influence conservation outcomes through the political process, there is no need for a more rapid and direct approach of markets. This assumes that DoC managers have a superior understanding of conservation priorities, and that any public involvement should not influence the relative evaluations of DoC's priorities. If DoC believes that its brief is to safeguard conservation that is not appreciated by the public, then it should hand over conservation that the public does want to community and private management.

The current allocation of mammal control further illustrates these issues. On what criteria is 25 per cent of the public conservation estate chosen for possum and goat control? Saunders (1998:33) claims that the areas for full herbivore and predator control (mainland islands) are chosen in the light of 'scientific and management objectives'. That all these areas are remote from the large cities (although two are on tourist routes) suggests that a customer orientation or public access is certainly not a criterion: so much for 'the birthright of New Zealanders' in the lower socio-economic groups that the Minister professes to care about in his press release.

DoC's rejection of multiple use and net conservation benefit are good examples of its outdated mentality. Multiple use before DoC was set up in 1987, and as practised in some US parks, meant that extractive or destructive uses sat together with non-extractive and passive use. Without a clear guideline of sustainability, the result was harmful to native ecosystems. For areas with high conservation value, such multiple uses pose major management challenges (see for example DoC, 1997c). With clearly articulated goals, it is possible to manage multiple-use mixes that have the potential to produce greatly enhanced conservation outcomes. For example, forest conservation areas are already managed for multiple uses such as wilderness recreation, erosion control, hunting, biodiversity conservation, and ecotourism. DoC could even heed Australian claims (Gottliebsen, 1998) that forests are carbon sinks that offset greenhouse gas-producing activities; in this way it could earn significant additional income for conservation. However, this would require management changes: a considerable part of the money would have to be used to control pests in order to reverse the current loss of carbon. Without control of both herbivorous and predatory mammals, the decline in native forest structure will result in a decline in carbon storage to a level below that achievable from rotation pine plan-

tations. Moreover, failure to accept that conservation is part of the market or that such an additional non-extractive use is part of conservation business would mean that government will claim any carbon credits from the public conservation estate and allocate them to industry. If conservation wishes to stand apart from the rest of the economy by failing to advocate earnings from conservation assets, then the only remaining option is government welfare.

Does the defensive reaction from DoC and conservation NGOs partly reflect the past actions of business? The current state of New Zealand's biodiversity shows that much of the country's prosperity has been won at the expense of the environment (Glasby, 1991). Hartley (1997:217) argues that 'conservation needs to be better integrated with the rest of the economy' and that 'other economic activities can often be altered slightly to deliver significant conservation benefits'. He provides little argument other than suggesting 'incentives' and the need to reconsider property rights. A full analysis of conservation strategies for New Zealand would have included an economic evaluation and discussion of the role that business and councils play in conservation. Some multinational corporations (such as Interface Inc.) have shown that business can promote conservation by integrating environmental sustainability into their business plans through programmes such as The Natural Step (see for example Hawken 1993).

Conclusion

Internationally, conservation organisations have faced similar criticisms to those levelled at DoC, and dealt with them in different ways. For example, the US National Parks Service, worried about managing public lands but seemingly delivering few public goods, in 1991 produced the Vail Agenda, a set of recommendations for future management (United States Parks Service, 1991). Unlike with past reviews and restructuring of DoC, large numbers of people were involved, over half of them came from outside the US Parks Service itself, and it was independently chaired. The debate over how best to fund the parks continues (Leal & Fretwell, 1997). The New South Wales National Parks Service has similarly announced a need to elaborate its vision for the next ten years through a public process. International agencies such as IUCN similarly argue for a need to re-evaluate conservation management and recommend economic approaches similar to those of Hartley.

New Zealand needs to undertake a similar project to establish a vision of conservation for New Zealand, preferably led by independent conservation professionals. The New Zealand government should commit itself to allowing the widest possible debate and to adopting the recommendations that are produced.

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End-Point Royalties for Plant Breeding in Australia

Ross Kingwell and Alistair Watson

PUBLICLY financed services to agricultural industries have been under review for some years (Baker et al., 1990; Watson et al., 1992; Industry Commission, 1994). Policy change has occurred in the public funding and provision of agricultural R&D and extension services (Cary, 1993; Godden, 1997). Change could be imminent in the publicly-funded provision of plant breeding services.

Australia's major broadacre industries are supported by mainly publicly financed plant breeding (Begg & Peacock, 1990). State governments finance plant breeding in State agricultural agencies and research institutes. Supporting funds come from the federal government that matches, up to a cap, farmers' levy payments on grain production. The Grains Research and Development Corporation (GRDC) administers these growers' and federal government contributions, and allocates some of the funds to providers of plant breeding services.

Plant breeding is subject to new legislation that enlarges and protects property rights in plant varieties. This enlargement of property rights may prompt change in the publicly financed provision of plant varieties for Australia's broadacre industries. The Plant Breeder's Rights Act 1994 extends intellectual property rights in plant varieties created in previous 1987 legislation.¹

The 1987 legislation had little effect on the breeding of broadacre crops in Australia because the intellectual property right in new varieties applied only to sales of seed to farmers. Returns to developers of new varieties were limited because the farmers who used the seed needed only to buy small amounts of it. Farmers who initially purchased these small amounts could then 'bulk up' (multiply) the seed and continue to use seed they had saved from the harvest of their own crops.² This farmer-saved seed was exempt from any royalty payments to the original developers of the variety. Because farmers save most of the seed they use in Australia's broad-

¹ See Godden (1998) for a full discussion of the 1987 and 1994 Acts.

² This applies to self-pollinated crops that are the main crops of broadacre farming in Australia.

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acre industries, returns to the commercial seed industry have been limited. But the 1994 legislation reduces this limitation by, in certain circumstances, extending the breeder's right to harvested material. This allows plant breeders to generate revenue by imposing on the sale of harvested material a royalty known as a 'product royalty' or 'end-point royalty' (EPR). An EPR is a levy imposed on the first sale of harvested material derived from varieties protected by plant breeder's rights.³

The main studies dealing with EPRs in the grains industry in Australia all treat EPRs as an option for increasing funds for plant breeding. But they display a variety of views about the desirability and practicality of introducing EPRs to support plant breeding.⁴ Most of them acknowledge the uncertainty over continued public investment in plant breeding for the grains industry, and suggest that it is possible and likely that public investment will decline in the future.

Will EPRs Hasten the Removal of Public Financing of Plant Breeding?

Godden (1998), comparing the findings of Lazenby (1986) and Clements et al. (1992), concludes that during 1985-92 the number of plant breeders for main broadacre crop species in Australia fell by 25 per cent, despite a 9 per cent real increase in finance from the GRDC. Watson (1997) observes that falling contributions from consolidated revenue are not being offset by increased revenue from the GRDC and industry partners, and that breeding programmes in several States are being abandoned.

Reporting on future options for crop breeding in Western Australia, ACIL (1997a:1) notes the government's desire to reduce its expenditure and to shift towards 'providing services with a high content of public good and community benefit, and away from areas where there is a large element of private good and individual benefit'. By contrast, Cook (1996) suggests that, apart from Western Australia, government financing of plant breeding is not falling to any significant extent. Cook considers that the introduction of EPRs will lead to withdrawal of public financing for plant breeding, and that those breeding programmes that could not finance themselves by EPRs will cease.

However, this is not a good argument for preventing the introduction of EPRs, since the public financing of plant breeding will be questioned regardless of whether EPRs are introduced. Already there is evidence, in the absence of EPRs, that budgetary pressures are restricting public financing of plant breeding. It is increasingly clear that in small countries like New Zealand and Australia farmers are the principal beneficiaries of varietal development, particularly yield improvement. Because international markets set grain prices, and states or regions are small participants in grain export markets, most financial benefits of regional varietal improvement through breeding are captured by farmers. The principle that beneficiaries

³ It is possible to impose a levy that is a product royalty without dependence on plant breeders' rights. However, the discussion here is restricted to EPRs that stem from breeders' rights.

⁴ See Cook (1996), Watson (1997), Hamblin (1997) and ACIL (1997a, b).

should pay requires that the financing of plant breeding should rely more on R&D levies on farm products and EPRs.

The introduction of EPRs may also stimulate private firms to enter breeding in their own right. However, the high set-up costs and the long delay between initial investment and generation of royalties from varietal adoption will deter many private investors. Private investors are more likely to emerge as equity partners with publicly financed organisations, which may see such partnerships as providing opportunities for reducing support for plant breeding from general taxation.

The crucial issue is the appropriate equitable mix of financing and management that delivers efficient social outcomes from plant breeding. Withdrawal of all public financing for plant breeding would be difficult to justify, as would failure to introduce mechanisms like EPRs that ensured that growers, as principal beneficiaries of varietal improvement, contributed more to plant breeding. As well, EPRs offer a property right or market-based solution to the provision of plant varieties and allow scarce public finances to be reallocated to higher priority areas.

Cooperation Between Plant-Breeding Organisations

Cook (1996) argues that, because EPRs would introduce commercial considerations into plant breeding, plant breeding organisations would cooperate less. This would affect not only the interchange of genetic material but also the sharing of knowledge about germplasm, plant-breeding techniques and breeding goals.

If EPRs are introduced, their effect on cooperation between host organisations will be influenced by the financing sources of those organisations. Over the last decade the GRDC has become a major financer of plant breeding in Australia. It has encouraged greater cooperation between host organisations and has responded to the lack of coordination across State boundaries and organisations identified in various reviews of plant breeding (Clements et al., 1992; Leslie et al., 1997).

So long as the GRDC remains a substantial financer or equity partner in regional breeding programmes that generate revenue from EPRs, then conditions on GRDC support for plant breeding within host organisations will ensure cooperation between organisations. However, if regional breeding programmes become privatised or national financers such as the GRDC have inadequate influence over the programmes, host organisations may well cooperate less, and the cooperation will become formalised through negotiated contracts and partnership agreements.

Where access to substantial flows of EPRs is at stake, this would provide incentive for some organisations to cooperate as a means of sharing in the EPRs. But in other cases, cooperation between organisations could be made more difficult by competition over access to EPRs, or more costly by the need to bargain over equity shares in collaborative agreements. Since reduced cooperation could impair the rate of varietal improvement, it is important that EPRs be introduced within a financing, equity and management framework that provides incentives or directives for the maintenance of desirable cooperation between organisations. In practice, the introduction of EPRs will increase the R&D funds of the GRDC because of its past and current equity participation in varietal development, assuming there is no

decline in R&D levies currently paid by grain growers to the GRDC. The larger pool of R&D funds held by the GRDC will increase its influence over grains industry R&D, particularly in regions contributing EPRs. Hence, if the GRDC adopts an overseeing role in supporting and coordinating plant breeding, it could ensure that cooperation between organisations continues.

EPRs and Plant-Breeding Programmes of Main Broadacre Crops

Hamblin (1997) expects that EPRs will sustain the breeding programmes of Australia's main broadacre crops, and that a shift will occur away from publicly financed plant breeding. ACIL (1997b) sees EPRs as essential to the survival of a well-resourced plant breeding effort in Western Australia.

However, several preconditions must be met if plant breeding programmes are to rely on EPRs as a main source of financing. First, the organisations that provide new varieties must develop varieties that will be adopted widely. Failure to do so will jeopardise the organisations' future because of limited future financing through EPRs.

Second, the organisations and their equity partners, if any, will need to re-invest some revenue from EPRs into plant breeding. Conceivably, some equity partners with national agendas may at times switch income from one organisation or region to another. As well, some organisations may re-invest EPR revenues in other areas of their R&D portfolio. Such uncertainty in the availability of funds may cause problems in planning and undertaking varietal development.

Third, the organisations must be able to judge whether royalty rates should differ between varieties, whether royalties should change over time and whether flat-rate or ad valorem royalties should apply. Risk management of the variable revenue stream from EPRs will also be important. Such variability contrasts with current public financing of plant breeding.

Public financing is provided mainly by central agencies (State treasuries) that provide plant breeding organisations with current and outyear financing intentions. Although forecast and actual levels of finance may differ, often the difference is not extreme, with allocations changing by less than 5 per cent in real terms from year to year. Admittedly, the internal allocation of finance to plant breeding within the organisations may be subject to greater variation, but plant breeding is often seen as a priority area of financing, which protects it from marked changes.

Further, the GRDC is a significant financer of plant breeding for agriculture. The level of its commitment varies across crops and regions, but it gives plant breeding a high priority and ensures that several plant breeding programmes have reliable financing. In Western Australia, for example, the GRDC allocates around \$3m annually to crop improvement, or 30 per cent of the expenditure within that State on crop improvement (ACIL, 1997b).

In contrast, EPRs are a more variable source of financing for plant breeding, since royalty payments are affected by crop production, crop prices and the degree to which growers adopt varieties subject to EPRs. For example, in years with prospects of low (high) yields or prices, farmers reduce (increase) the area they give over

to crops. Hence, breeding organisations that wish to rely solely or mainly on EPRs will need to establish and manage reserve funds, implement optimal borrowing and/or investment strategies and decide on EPR rates.

Niche or Specialty Varieties

Cook (1996) considers that EPRs will privatise the market for new plant varieties, leading to the neglect of specialty and niche market varieties. But Watson (1997) believes that such neglect is a minor problem because niche markets are by definition small. Whether introduction of EPRs would cause the neglect of varietal development for niche markets depends on the level of finance available to plant breeding; on the relative returns to investing in breeding of major crops as opposed to minor or niche crops; and on the desired outcomes of financing from equity partners in plant breeding.

However, where plant breeding for niche crops or markets is financed largely through EPRs and is unprofitable, varietal development will not necessarily cease. In these situations, affected growers may choose to support agronomic or plant breeding activity through voluntary financing arrangements, as they do for oats in South Australia and for noodle wheats in Western Australia.

Cosmetic Breeding

Another of Cook's (1996) concerns is that EPRs will encourage waste, with excessive investment in promotion and packaging and inadequate investment in substance. Yet studies of crop and varietal adoption have found that farmers' beliefs about the yield advantage and profitability of varietal changeover significantly influence their adoption decisions (Lindner & Gibbs, 1985; Abadi et al., 1996; Abadi & Pannell, 1998). Several other factors are relevant: farmers' long association with varietal replacement would alert them to cosmetic changes; it would be unwise for a breeding organisation to risk its reputation by developing cosmetic varieties that impose changeover costs on farmers yet deliver no yield or price benefits to them; and if the equity partners in breeding organisations included farmer representatives, these farmers would discourage cosmetic activity that delivered no monetary benefit to growers.

Germplasm Development

Cook (1996:11) argues that germplasm development 'is expensive, long term, and is likely to be an early victim of the introduction of product royalties'. Wright (1996), in his account of the extent of germplasm development in public and private breeding programmes in various parts of the world, finds that many public and privately financed breeding programmes depend on a narrow range of the available germplasm. However, as Allard (1992:144-5) points out:

Breeding in barley and corn, as well as in other major crops, has increasingly focused on crosses among elite materials and rates of progress indi-

cate not only that this strategy has been successful but also there has been little, if any, slowing of progress due to reduction of exploitable genetic material. ... It consequently seems unlikely that readily exploitable genetic variability will soon be exhausted.

It is debatable whether the narrow range of germplasm in many breeding programmes represents an appropriate outcome of the search for desirable traits or indicates under-investment in germplasm development.

Cook's concern is that the introduction of EPRs will result in less finance for germplasm development. Whether this occurred would depend on the overall level of finance available to plant breeding through EPRs and other sources and on the relative returns to investing in the long-term development of germplasm as opposed to the short-term focus on using existing elite lines as parental material. If EPRs made possible an overall increase in finance for plant breeding, investment in germplasm development would not necessarily be a casualty of change. Further, some stakeholders in plant breeding are concerned with the economic and ecological sustainability of plant breeding activity, and would therefore ensure commitment to germplasm diversity and development. In addition, genetic engineering technology will facilitate a widening of the germplasm base of prospective varieties by allowing desirable genetic traits to be incorporated more quickly in parental material.

Admittedly, if EPRs are the sole or dominant source of funds for plant breeding, and if current stakeholders in plant breeding are displaced by private firms managed for short-term profit, then investment in germplasm development is likely to wither. Since current markets do not convey appropriately the value of future desirable varietal traits that reside in currently untapped germplasm, there is a need for preservation and conservation of germplasm.

The introduction of EPRs may make it possible for public funds currently devoted to plant breeding to be diverted to germplasm development and conservation. On the other hand, it may also facilitate privatisation of breeding activity, with government also withdrawing support for related activity such as germplasm development. It needs to be stressed that EPRs, although extending an intellectual property right in varieties, do not redress completely the market failure associated with germplasm development and conservation.

Linking EPRs to Investment in Breeding

Both Cook (1996) and Watson (1997) observe that there is no requirement or certainty that EPR revenue would be returned directly to support plant breeding. By contrast, Hamblin (1997) implies that EPRs will directly support plant breeding. Watson (1997:17) notes that 'Paying the owners of cultivars some of the proceeds of levies collected for research does not guarantee that these funds will be spent on plant breeding in the future'. There are various ways to ensure that EPRs support further plant improvement. Certainly, the politics of introducing EPRs suggests that farmers would accept EPRs more readily if they were confident that mechanisms existed to ensure that royalties supported further plant breeding. If organisations

developing varieties depended on equity partnerships with growers, growers would ensure that EPRs supported plant breeding.

In neither the public nor the private sector is there any certainty that all EPR revenues will flow to support plant breeding. Usually, public sector host organisations are subject to government intellectual property policies that require a return of revenue share to State treasuries. In the private sector, large companies will direct some EPR revenue as dividends to shareholders; and income from EPRs could be used to finance other ventures unrelated to plant breeding. Even where support for plant breeding continues, it could flow to plant breeding in other regions or countries that offers greater returns.

Development of Varieties with Only Quality or Price Premia

Watson (1997:23) argues that 'product royalties cannot handle spillovers between crops as efficiently as the current system', leading to the development of varieties that offer quality or price premia rather than farming system or agronomic advantages. This argument is valid, especially in cases where breeding activity is solely or mainly financed through EPRs and is undertaken by private firms with limited species portfolios in their breeding programmes. Take the case of grain and pasture legumes that bestow a range of rotational benefits to following cereal crops (Ewing et al., 1987). Legume breeders are aware that the adoption by farmers of a new legume variety depends not only on how it performs with respect to its yield and quality, but also on the rotational benefits it promotes (Abadi et al., 1996).

However, EPRs flowing to legume breeders would be based only on sales of harvested legume grain subsequently sold. Further, because grain legumes are used widely on farms as animal feed, a significant portion of production may escape payment of an EPR. Hence, if the breeding of the grain legume were to depend mainly on EPRs, it would be difficult not only to generate a level of EPR revenue commensurate with the benefits farmers derived from using the variety, but also to establish an equitable EPR. The latter difficulty arises where legume breeders impose a high rate of royalty in the hope of increasing EPR revenue to compensate for forgone EPRs on legume production. The high rate of royalty will lead farmers whose production attracts an EPR to consider it inequitable that other farmers are free-riding through having greater access to grain that escapes EPR payment.

The introduction of EPRs will also complicate plant-breeding investment decisions in species that offer farming system or rotational benefits, as well as yield and quality improvements. The current system of production levies, disbursed by bodies such as the GRDC with its national priorities and partnerships with State agencies, is better able to allocate appropriate finance to support a range of plant breeding activity for these species than finance based on EPRs.

EPR Collection

Both Watson (1997) and Cook (1996) foreshadow problems in EPR collection, and point out that EPR collection would require costly varietal identification. ACIL

(1997b), however, reports a feasible, relatively inexpensive collection system for Western Australia, and finds that the cost of varietal identification is not as costly as claimed.

The cost of compliance reflects several factors, such as grower acceptance of EPRs, increased income through adopting varieties subject to EPRs, and whether or not varieties differ in their royalty rate. Lazenby et al. (1994) find that less than 2 per cent of varieties delivered by farmers were wrongly named, and conclude that the incidence of false declaration has probably been exaggerated. However, this degree of compliance may not continue with EPRs, which initially will provide growers with a greater incentive to make false declarations. Increased testing for varietal compliance may need to accompany the introduction of EPRs.

A further problem is that harvested grain may escape EPR collection. For example, grain retained on-farm for use as animal feed, or sale of grain by farmers to their neighbours, will mostly escape EPR payment. In regions where a large proportion of grain is retained on-farm and EPRs are the sole source of finance for plant breeding, the reduced effectiveness of EPR collection will reduce the level of breeding.

Effects on the Adoption of New Varieties

Hamblin (1997) notes that the introduction of EPRs will lower the cost of seed. In a related comment, Watson (1997) observes that EPRs are preferred by the commercial seed industry as a means of encouraging adoption of new varieties. Both authors note that EPRs facilitate adoption by shifting part of the risk of new varieties from the farmer to the breeder. Lazenby et al. (1994) agree that EPRs would encourage the more rapid adoption of new varieties.

Without EPRs, varietal release procedures in many mainly publicly financed organisations involve calling for tenders for seed bulk-up. Usually a variety is released to only a few tenderers, who pay for the exclusive right to bulk-up the seed and subsequently profit from seed sales. Payments by tenderers help finance plant breeding. Competitive tendering arguably limits the early adoption of a variety because of the higher seed prices charged by tenderers who need at least to recoup tendering and bulk-up costs. However, introduction of EPRs could enable varietal release procedures to change and become less reliant on tender income.

With EPRs, the commercial interest of those releasing a variety can be best served by the early and widespread adoption of the variety. Firms could be paid by the plant breeding organisation to bulk-up seed. In this case, EPRs facilitate early adoption of a variety because breeding programmes would dispense with the need to gain revenue through the tender process for seed bulk-up. However, an EPR could deleteriously affect varietal adoption. When EPRs were introduced, new varieties attracting an EPR would be competing for market share against older varieties not subject to an EPR. As a result of the presence of an EPR, the new variety would need to offer yield and quality improvements whose expected values exceeded the costs of varietal changeover, including the payment of EPRs. Hence, initial adoption of varieties subject to EPRs would be less than when almost all va-

ieties sown are subject to EPRs. However, even when most farmers are sowing varieties subject to EPR, adoption would be impeded if the EPR rate on a new variety is set too high.

Farmers' and Breeders' Objectives

Hamblin (1997) argues that EPRs will lead to greater synergy between farmers' and breeders' objectives. The financing of future plant breeding will depend on breeders developing varieties that are widely demanded. Breeders will therefore face strong commercial incentives to develop varieties that are quickly and widely adopted.

Yet such greater synergy may in practice be difficult to achieve. Varietal development has long lead times, with breeders selecting parents and making early selections that affect traits available in prospective varieties a decade later. While it is clear which plant traits farmers prefer today, it is not clear which varieties and traits they will prefer in a decade's time. This uncertainty limits the synergy between farmer and breeder objectives. In practice, most breeders maintain a cohort of material through many stages of their breeding programmes. This provides diversity for selection when and if economic or agronomic changes call for changes in required traits.

Concluding Remarks

Whereas all the main studies of EPRs identify some problems in relying on them, they differ in their final assessments. Cook (1996:14) concludes:

Both the current system of funding broadacre crop plant breeding, and the proposal to fund it through product royalties, have advantages and disadvantages. Those of the current system are clear, and comparatively well known. Those of the product royalty system are much less clear, and subject to speculation and special pleading.

In similar vein, Watson (1997:2) concludes: 'While end-point royalties are still a useful way of increasing funds available for plant breeding, there are conceptual and administrative problems'. However, 'Despite these difficulties, end-point royalties can be useful for minor crops and where marketing channels are concentrated, for major crops'. On the other hand, Hamblin (1997:2) believes that something like EPRs are a necessary response to a likely decline in public financing of plant breeding for agriculture. And ACIL (1997b:2) concludes that EPRs 'have the potential to provide substantial financing levels to plant improvement activities but seasonal variations and competition from other plant breeding organisations will provide some limitations on this source of revenue'.

The introduction or extension of any new property right, such as plant breeder's rights that underpin EPR collection, requires a legal, policy and management framework in which these rights can function properly. In the case of EPRs, a

badly designed framework could lead to inappropriate levels, types or structures of investment in plant breeding, and a sub-optimal level of plant improvement .

If EPRs become the sole source of financing plant breeding for Australia's broadacre crops, and breeding becomes privatised, there is a risk of some crops or regions becoming disadvantaged. Crops or plant species with either spillover benefits or characteristics that make EPR collection difficult risk under-investment in their germplasm protection and development and under-investment in their plant breeding. Introducing EPRs may inhibit cooperation between some plant breeding organisations. Accordingly, the role of the GRDC is crucial. Its equity or financing participation in plant breeding and its national mandate could ensure that policy, management and financing of plant breeding address such potential deficiencies. If the GRDC adopts an overseeing role in supporting and coordinating plant breeding in the grains industry, it could ensure that potential deficiencies of EPRs are lessened.

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Development and Democratisation in East and Southeast Asia

Jamie Mackie

A broadly positive correlation can be observed throughout the world (although there are several significant exceptions) between various countries' levels of economic development and their degree of progress towards democratic institutions (Lipset, 1959, 1960; Huntington, 1991). But in Southeast Asia the exceptions are so striking as to disallow us from simply assuming that the one causes the other.¹ The connections are much more complex than that, and the theoretical assumptions involved as well as the empirical data demanding explanation turn out to be tangled up with other factors as well.

'The more well-to-do a nation, the greater the chances it will sustain democracy', wrote Lipset (1960:48-50) about the more advanced industrial countries in the early years of debate on this topic. Much the same has been said about the developing countries since the 1970s, most notably the fast-growing nations of South-east and East Asia, in contrast with the poorer countries of Africa and elsewhere, most of which (apart from India) are not very democratic at all (Morley, 1993/1998; Friedman, 1994; Linz & Stepan, 1996). But correlation does not in itself signify causation.

The central issue is why steps towards more democratic government (as defined below) have occurred in some countries in East and Southeast Asia over the last 40 years as they have become wealthier and generated a larger, more influential middle class, whereas in others no such political change has resulted from rapid growth, despite the emergence of large middle classes. The broader theoretical issues that have arisen in the now extensive literature on this subject can only be touched on briefly here. Essentially, this article seeks to answer several questions that are often asked in this context. Is rapid growth conducive towards democratisation in all circumstances, or do other factors also come into play? Or does the converse apply: that is, that authoritarian governments or strong states, capable of curbing civil and political liberties, are essential to get the growth process started? Or is there an element of truth in both these propositions (as I will argue, with qualifications on both counts), and if so, how are the two to be related or distinguished? The impact and extent of the 1997-98 financial crisis will have to be left out of consideration, as

¹ The connection may be closer in Northeast Asia, apart from China and North Korea.

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will unwarranted occasional assertions that the growth achieved in the years before then was not real or rapid, even though flaws were already visible behind the supposed 'economic miracle' in all countries of the region, including Japan. As well, China and the other highly authoritarian communist states of the region will be left out of account here, as will the two maverick cases of Myanmar (Burma) and Brunei.

No Simple Link

Taiwan and South Korea were certainly authoritarian regimes in the earlier phases of their post-independence economic development. A causal connection seems to have been at work, since the two strong state systems were able to get rapid growth started well before most other countries, for reasons outlined below. After experiencing rapid economic growth for over 20 years, each country developed a large middle class which played a major part in the struggles in the 1980s to achieve more democratic institutions, which now seem to be securely established. Thailand was also an authoritarian regime at the time when its rapid growth phase started in the 1950-60s, although it was never such a 'strong' state as Taiwan and South Korea. It too began to change gradually towards a more democratic form of government from the mid-1970s onwards, especially during its 1986-96 boom years. The gradual consolidation of its political parties and parliamentary system, though badly flawed by 'money politics', was sufficient to defeat a military *coup d'état* in 1992 and to establish party-based parliamentary governments since then.

Japan, on the other hand, has, throughout its five decades of astonishingly rapid growth, had a formally democratic set of political institutions, which were imposed under the postwar US occupation. Yet its system of government could not be said to have become significantly more responsive to social demands and pressures during that time, or more democratic or participatory, or capable of curbing the immense power of the bureaucracy. Likewise, Malaysia and Singapore have long had the formal trappings of democracy which they inherited as British colonies about 40 years ago; but the actual practice of representative government there has not become in any sense more democratic as they have grown wealthier: if anything, the reverse. Singapore is in practice a highly authoritarian one-party regime, and Malaysia semi-democratic, or 'responsive-authoritarian' (Crouch, 1996) at best, despite their high growth rates, the highest per capita income levels in Southeast Asia, and large middle classes. The Philippines also inherited a set of democratic institutions, on a US-style congressional model, with parties and regular elections; yet it has experienced fluctuations towards a dictatorship under Ferdinand Marcos (1972-86) and back towards a rather chaotic, ineffectual democratic regime since then, thus defying any clear-cut generalisation about the links between growth and democracy.

Indonesia has been the most striking exception to any such proposition, for its rapid economic growth during 1966-97 gave rise to an immense increase in the power of the state, largely concentrated in the hands of President Suharto himself, within a highly personal and patrimonialist system of government and at the ex-

pense of the civil society. Hence, growth has been accompanied there by a weakening of representative institutions (the word democracy is hardly relevant in the Indonesian context) rather than the reverse.

From this bald survey, it is clear that no simple link is discernible between economic development and democratisation in the fast-growth countries of eastern Asia. While there is some evidence in favour of such a proposition in the cases of Taiwan, South Korea and Thailand, the opposite is the case for Indonesia, Singapore and Malaysia. Other variables have to be taken into account in each case.

'Democracy' and 'Democratisation'

Something more must be said at this point about the meaning attributed here to terms like 'democracy' and 'democratisation'. (The latter is less problematic since it simply means a process of change broadly in the direction of democracy.) Both terms are used here loosely and generally, descriptively rather than normatively, to indicate how nearly any particular regime approximates to an ideally democratic system of government in which the executive power is responsive to the views, preferences and demands of the people, as expressed through institutions such as elections, political parties, a parliament or congress and a set of rules to ensure that the executive is periodically accountable to the parliament or the people. The cases of Singapore, Malaysia and Japan, as mentioned above, which all appeal to values other than those of conventional Western 'liberal democracy', indicate clearly that it is not just the presence or absence of those institutions that matters most but the ways in which formally democratic institutions actually work. Equally important are the more deeply rooted social attitudes and values which imbue them, particularly on issues such as freedom of expression and the press, the autonomy of the courts, the beliefs of both governments and citizens about human rights, legal and civil rights and obligations, and ideas about the individual and the community, society and state, all of which vary widely throughout the developing world.

The term 'illiberal democracies' has been coined by Fareed Zakaria (1997) to refer to regimes (mainly in the Balkans, Africa and Central Asia, but applicable also to some Southeast Asian countries) that hold free elections but do not respect the rights of their citizens. Zakaria (1997) urges a greater emphasis on reviving constitutionalism and the rule of law rather than the 'fixation on ballot boxes' (Kupchan, 1998:122). Yet according to Kupchan, 'the current wave of democratisation is taking place in regions which have little or no experience in constitutional liberalism' but rather 'a long history of paternalism and social norms that privilege the group over the individual'. Kupchan disagrees with Zakaria's advocacy of promoting constitutionalism before democracy, arguing that liberalism has preceded democracy only in the Anglo-Saxon West where 'political culture, practices and institutions were already imbued with the spirit of constitutional liberalism' long before democracy took root there. He urges that even an imperfect democracy can serve 'as a beachhead for liberal values, not vice versa' and that 'illiberal democracy may be a way station along the road to more benign forms of government ... from autocracy towards liberalising autocracy, and in some cases towards liberalising semi-

democracy' (1998:123). This aspect of the subject, though a most important one, cannot be adequately explored here, for the related question of 'Asian values' in all this is a complex and subtle one. But it should be kept in mind as we explore the factors involved in whatever explanatory model may be advanced about economic growth and progress towards democratisation.

Is Authoritarianism a Necessary Condition of Growth?

The proposition that strong government and curbs on civil and political liberties were essential for initiating growth rested on the belief that only an authoritarian regime could impose unpopular but necessary policies involving industrial discipline, resistance to high wage levels, suppression of militant trade unions and peasant organisations: in short, insulation from the demands of special interest groups. High levels of governmental autonomy seemed to be necessary in the early stages of growth and 'primitive accumulation of capital' in order to avoid the weaknesses of what Gunnar Myrdal (1968) called 'soft states' without an effective capacity to carry out the policies they ordained. South Korea and Taiwan were the examples most commonly cited in favour of this view in the 1960-70s, with Singapore under Lee Kuan Yew and Indonesia under Suharto later being added to the list, as well as the Philippines under the Marcos dictatorship of 1972-86 (but the Philippines had the highest income levels in Southeast Asia and high rates of growth during the 25 years of democratic government before 1972).

Dependency theorists were inclined to use this sort of argument to support their belief that the ruling elites of those countries were being covertly manipulated by huge foreign multinational corporations which were thought to be acting in collusion with the elites to advance the interests of both parties at the expense of the rest of the population (the workers and peasants in particular) so as to enmesh the economies of those countries into the global capitalist system. There was a grain of truth in that argument, although the cruder claims about the dominance of foreign capital and subservience of the state to it were later seen to be misleading. Singapore, for example, has relied heavily on foreign capital, yet the Peoples Action Party government has proved to be highly autonomous, insulated from society-based pressure groups, patently not the servant of either multinational corporations or domestic capitalists but their master. In the early stages of development of Taiwan and South Korea, foreign direct investment played a relatively small part (although foreign aid from the US and overseas loans were crucial) and the governments of those countries were highly autonomous.

More sophisticated variants on the growth-authoritarianism theme emerged in the 1980s with Chalmers Johnson's (1987) influential 'developmental state' theory, based on his interpretation of the structural basis of rapid growth in Japan and the newly industrialising countries (NICs) South Korea, Taiwan, Singapore and Hong Kong (a very disparate array of politico-economic systems), and an interpretation in terms of 'growth coalitions' as the political basis of fast growth in those countries by Stephan Haggard and Cheng Tun-jen (1987).

Johnson's idea of the 'developmental state' was not concerned directly either with the authoritarianism-democratisation debate (for the prospects of democratisation would have seemed bleak in Taiwan and South Korea when he first used the term in 1981) regarding necessary and sufficient conditions for development, or with the growth-democratisation nexus, so much as with the question of how the political elites in those countries had avoided capture by their major clients, especially privately owned big business. But he did stress the 'strong state' feature of these countries in the course of showing the importance of government intervention in economic life in Japan, South Korea and Taiwan, contrary to the views of *laissez-faire* economists who stressed only on their reliance on market forces and export-oriented economic policies. But the model he advanced also focused on four main elements behind the economic success of the Asian NICs:

stable rule by a political-bureaucratic elite not acceding to political demands which would have undermined economic growth; cooperation between public and private sectors under the overall guidance of a pilot planning agency; heavy and continuing investment in education for everyone, combined with policies to ensure equitable distribution of the wealth created by high-speed growth; and a government that understands the need to use and respect the methods of economic intervention based on the price mechanism. (Johnson, 1987:145)

Haggard and Cheng (1987) put forward a less muscle-bound variant of the developmental state theory in their study of Taiwan, South Korea, Hong Kong and Singapore, the then generally accepted group of Asian NICs. They too stressed the 'insulated' character of the state in all four NICs, but put more emphasis than Johnson did on the part played also by repression of workers and labour organisations. Their main contribution was to show how various 'growth coalitions' within elite and business circles had come to reject import-substituting industry policies and to support export-oriented growth based on market-conforming modes of government intervention in economic life. They drew on dependency theory in their stress on the triangular relationship between the domestic bourgeoisie, foreign capital and the state as the key players determining the formulation of export-led growth strategies. But they were not the prisoners either of old Marxist assumptions that the economic success of these countries was due mainly to the exploitation of the workers through low wage levels, or of the dependency-theory belief that the governments and business elites of these countries were hand-in-glove with foreign capitalists to whom they were beholden. The value of their approach to the analysis of the socio-political dynamics of economic policy-making in the NICs lay in providing an account of the relatively autonomous 'strong' state which led towards a more flexible and nuanced view of the relationship between state and society in these countries. This approach was not invalidated when Taiwan and South Korea suddenly and surprisingly shifted towards more democratic regimes in 1985-87, for the study of the state-society balance and business-government relations in the processes of eco-

conomic policy-making which flowed out of their work has become much more diverse, flexible and illuminating not only for those two countries but also for others in the region.

Yet applying either the 'developmental state' or the 'growth coalitions' approach to Southeast Asia creates difficulties, quite apart from the special problems posed by Singapore as a Southeast Asian NIC (Mackie, 1988). For example, Thailand, formerly considered the archetypal 'bureaucratic polity' which was highly insulated from social pressures, could not be accurately described in terms of Johnson's developmental state theory even in the years of intensely authoritarian rule by military juntas before 1973. Subsequently, its phases of most rapid economic growth have occurred since the 'democratic interlude' of 1973-76 and the decline in state autonomy. That was followed, after a brief phase of return to military rule, by gradual steps towards democratisation and rejection of military intervention in government during the 1980s under General Prem Tinsulanond, especially during the boom years 1986-96. The government and its policies were never dominated by US or Japanese private capital, even though foreign direct investment rose steadily during that period and then very rapidly after 1986 (Pasuk & Baker, 1996). Likewise, Malaysia has never had an especially 'strong', authoritarian or 'insulated' state since independence, although it has at best been only a semi-democratic one; yet it has had steadily high growth rates ever since the late 1950s (Crouch, 1996). Wages have not been kept low there, as in the developmental state model, and the influence of British capital has declined steadily since the 1970s. The Philippines and Indonesia have had even more complex patterns of economic and political development since 1945, which can be explained only in terms of their particular circumstances, in defiance of dependency theory or developmental state models rather than in accordance with them (Mackie, 1993/1998).

Thus we are left with two unresolved problems here — and perhaps others that flow from them. First, if it is not the case that highly authoritarian regimes have been more easily able to get growth started than relatively democratic ones (however we may define these terms; it is better to think of them loosely as opposite poles of a spectrum rather than as sharply dichotomous), what *are* the political underpinnings of economic growth? This is not the place to go into that question at any length, since it is the obverse of our primary concern here, which is with the political *consequences* of growth, not its causes or preconditions. I have tried to investigate the latter elsewhere (Mackie, 1988) with reference to the (then) ASEAN states, but it is sufficient simply to note one very general observation here.

Authoritarian states have obviously *not* been successful in generating growth in many countries in Africa, the Middle East and elsewhere, while several in the Asia-Pacific region have successfully achieved high growth rates without having highly authoritarian regimes (Thailand most obviously, Malaysia and the Philippines less so). But while authoritarian government may not be a sufficient condition for rapid growth to occur, it may arguably be a necessary condition for getting the growth process started, by enabling governments to hold down wage levels, generate high savings and investment levels, and direct scarce capital towards infrastructure and

human capital rather than consumption. It is hard to identify any countries which have achieved high growth rates without relatively authoritarian regimes, apart from the rather special case of the Philippines in the 1950-60s, where the role of US capital, aid and policy advice was substantial.

But perhaps it was not authoritarianism as such that was critical to the initial growth process so much as 'insulated' or autonomous governments and a high degree of bureaucratic competence. Equally important may have been the ability of governments in Taiwan, South Korea and Singapore to avoid 'capture' by either rent-seeking business firms or radical unions, and so to enforce the rules of the game that kept markets competitive and a level playing field). Those conditions did not apply in the Philippines under Marcos, or in Indonesia under Suharto, although markets were liberalised to some extent and growth generated at lower levels. Malaysia benefited from a very competent bureaucratic structure, a relatively open trade regime, and not too much 'capture' by special interest groups in the early stages of development.

Second, what can be said about the links, if any, between economic growth and pressures for democratic reform, whether successful or not, from various elements within the society? I want to approach this question by, first, examining the importance of the middle class as a key element in the socio-political chemistry involved; second, by touching briefly on Samuel Huntington's analysis of the post-1970 'Third Wave' of transitions from authoritarian to democratic regimes throughout the world; and finally by turning to the problems of applying this kind of explanation to the five original ASEAN countries.

Growth, the Middle Class and Democratisation

It is commonly asserted that democratising tendencies in developing countries are due wholly or largely to the growth of a middle class, educated, urbanised and bound up with the modern world, upholding the prevailing ideas and (in part) ideologies of their counterparts in more advanced industrialised societies. Members of the middle class have a stronger interest than most other social groups in pressing authoritarian regimes to widen and strengthen the civil liberties of their citizens, to minimise the arbitrary authority of officialdom or the military, and to move towards a rule-based administration and the rule of law. Even if they do not go so far as to press strongly for fully 'democratic' forms of government (for they may find themselves outvoted by the workers or peasants in a genuinely democratic electoral system, or severely repressed by military or right-wing elements in authoritarian regimes if they push too far), they are likely to be broadly in favour of reforms in the direction of a more accountable executive power that is responsive to pressures from social groups, if only to cope with the greater complexity of policy-making in an increasingly industrialised society. But while the strength of middle class elements in developing countries may be correlated to some extent with the levels of industrialisation, urbanisation and education prevailing in a particular country, we cannot assume there is an automatic or inevitable process at work here which leads towards a strengthening of democratisation tendencies. The Philippines, for in-

stance, had by far the largest and best educated middle class in Southeast Asia in the 1960s at the very time when Marcos plunged the country into martial law and a highly regressive dictatorship, with surprisingly little effective resistance from the middle class (and even much support).

The various studies of 'transitions from authoritarianism' by O'Donnell, Schmitter and Whitehead (1986), mostly in southern Europe or South America, were of value in pointing beyond simplistic generalisations about the growth of a middle class as a factor in democratisation towards the interactions and negotiating processes that take place within authoritarian regimes between various political actors both inside and outside the state structure who are involved in struggles to alter or retain the status quo. They were particularly good in their analysis of the complex politics of negotiation there between the *duros* and *blancos* (hard-liners and soft-liners) as to the choice of repressive or accommodating policies towards opponents of the state. In nearly all cases where transitions from authoritarian rule have occurred, the rifts between *duros* and *blancos* have at times provided enough scope for the advocates of change to be able to drive wedges between them and make limited gains in the direction of more democratic political institutions.

Just as the widespread failures of democratic systems in developing countries in the years after 1958 and the emergence of authoritarian regimes there attracted a lot of attention among Western political scientists at that time, the pendulum has swung in the opposite direction since the 1970s. Huntington's (1991) 'Third Wave' study of the circumstances surrounding the numerous shifts towards democratic governments throughout the world since about 1970 provides one of the most comprehensive studies of the various factors which help to account for this trend across the world, of which economic growth and the emergence of an educated middle class are merely two, and not necessarily the most decisive ones. Like the 'transitions' analysts, Huntington highlights the roles played by political actors on both sides, as well as the prevailing economic circumstances within which they had to act. On the relevance of levels of economic development to the probability of achieving democratic reforms, he observes that:

Very rapid economic growth inevitably produced challenges for authoritarian leaders. It did not necessarily lead them to introduce democracy ... Over the long term, economic development creates the basis for democratic regimes. In the short term, very rapid economic growth and economic crises may undermine authoritarian regimes. If economic growth occurs without economic crisis democracy evolves slowly, as it did in nineteenth century Europe. If the destabilising growth or economic crisis occurs without the achievement of transition zone wealth, authoritarian regimes may fall, but their replacement with long-lived democratic regimes is highly problematic. In the third wave, the combination of substantial levels of economic development and short-term economic crisis or failure was the economic formula most favourable to the transition from authoritarian to democratic government. (Huntington, 1991:72)

While not very elegantly expressed, this extract does underline the important point that any search for correlations between growth and democratisation needs to look well beyond any simple one-to-one relationship towards, for example, the role of crises in destabilising authoritarian regimes (and thereby opening up opportunities for the advocates of democratisation) and the conditions determining the sustainability of democratic governments once they are established.

The Growth-Democratisation Nexus in Southeast Asia

In the most thorough and sustained enquiry yet made into the correlation between economic development and democratisation tendencies in the major countries of East and Southeast Asia, Crouch and Morley (1998) have shown that while Lipset's observation quoted earlier (that the wealthier a nation 'the greater the chances that it will sustain democracy') is broadly true of this region, there are some notable exceptions. Three of the four countries with the highest per capita income levels in the region in the 1990s — Japan, Taiwan and South Korea — are classified as 'consolidated democracies', while the fourth, Singapore, is categorised as 'authoritarian-responsive', even though its income levels are nearly twice those of Taiwan and three times South Korea's. At the other end of the scale, China, Vietnam and Myanmar, all still in the low-income category, have authoritarian regimes of various types. Of the middle-income countries, Malaysia, Thailand and the Philippines are classed as formally democratic, despite various imperfections, but Indonesia, the poorest of them, is regarded as 'authoritarian-military', despite its high growth rates over the last 30 years and despite the fact that it had earlier had more than a decade of vigorously democratic, party-based parliamentary government in the years 1945-59, at a time of much lower per capita income levels than in the 1990s.

One of the conclusions that Crouch and Morley (1998) draw is that:

It is not accidental that medium levels of economic growth are commonly associated with instability, most political regimes weaving between authoritarian structures and [merely] formal democracies, while the higher levels are generally correlated with democracy ... These correlations would appear to be in large part the effects of the growth process itself, mediated through the social and political processes it generates ...

Beyond this point, the analytical problem becomes partly a matter of explaining the anomalous cases of Singapore and Indonesia (and to a lesser extent Malaysia and the Philippines), while also depicting a more refined and flexible explanatory model for the observable patterns of socio-political change. Using what is essentially Karl Deutsch's notion of social mobilisation as a key element in the equation, Crouch and Morley (1998) have put forward a stylised explanation in terms of what they call the 'driven-by-growth model', subject to the assumption that all other factors are equal, which is a very important qualification (since they rarely are equal in this part of the world), as follows:

Economic development drives social mobilisation;
 Social mobilisation drives political mobilisation;
 Political mobilisation drives regime change.

Not all regime changes will result in democratisation, however, at least as it is understood in the West, and it would be erroneous to treat this 'model' in too deterministic a manner by implying that democratisation is an inevitable outcome of either economic development as such or the social or political mobilisation it generates. Other variables must also be brought into account, particularly ideologies, 'Asian values' and institutional factors such as the role of the armed forces, the strength or weakness of political parties, freedom of the press, the competence of bureaucracies, the autonomy of the judiciary and older traditions about individual freedom *vis-à-vis* the community.

Authoritarian regimes can be expected to respond to the pressures generated by social and political mobilisation in different ways, some moving towards more representative or democratic directions, other creating new institutions which will enable them to accommodate pressures from below without making concessions towards demands for democracy. Obvious examples of this are Singapore's resort to a quasi-one-party regime since 1965 and Indonesia's shift to a highly authoritarian 'Panca Sila democracy' based on the state-controlled Golkar organisation, the armed forces' civic-mission type 'dual function' and a highly conformist, patrimonialist political system. Moreover, specific local factors may also come into play in varying degrees, such as the ethnic cleavage in Malaysia, where the Malays have long feared they might become subordinated in their own land by the wealthy Chinese minority, or the acute sense of vulnerability felt by the Chinese in tiny Singapore. Hence:

The four anomalous cases do not ... contradict the argument that high economic development strengthens the forces leading towards democratisation. What they do show is that the impact of economic development must be weighed in the context of other forces, which may strengthen or weaken it ... Our analysis [is put forward] ... not as a formula for precise prediction, but as an instrument for sensitising one to some of the more potent forces with which we shall all have to grapple. (Crouch & Morley, 1998)

Among the 'other forces' which enter the equation as intermediate variables, according to Crouch and Morley, are geographical factors (varying from Singapore's extreme smallness and sense of vulnerability to China's immense size and Indonesia's potentially fissiparous character), political culture, deeply entrenched political institutions, elite cohesiveness, social factors such as communal divisions and social stratification, and vulnerability to external pressures. The influence of dominating personalities (Lee Kuan Yew, Suharto, Sukarno, Marcos and Mao Tse-tung most obviously, but several others too) has often been significant in directing their na-

tion's course towards either authoritarianism or democracy. Hence any enquiry into the strength of democratising forces in these countries must look beyond mere economic indicators like growth rates or per capita income levels, as if these were the key determinants, to take account of the intricacies of their history and politics also.

It is here that the various other issues raised in the studies by O'Donnell et al. (1986) of 'transitions from authoritarianism' also become relevant to any investigation into the issues under scrutiny here. They have not had much attention in the Southeast Asian context, however, not least because the only clear-cut examples of such transitions so far have been the overthrow of Marcos in the Philippines in 1986 (Mackie, 1993, 1998), of the military junta in Thailand in 1992, and of Suharto in 1998. A more fruitful approach to these matters in the various Southeast Asian countries may be along the lines of Haggard and Kaufmann's (1995) analysis of the relevance of institutional factors to regime change or survival, either authoritarian or democratic:

The ability of both authoritarian and democratic leaders to maintain power is a function of economic performance, which in turn is dependent on the conduct of economic policy. Institutions affect the coherence of policy both in the initiation phase, when executive authority is an asset, and during the consolidation phase when success rests on building bases of social support. (Haggard & Kaufmann, 1995:10)

This approach directs our attention to the sustainability of democratic institutions and processes after any transition from authoritarianism has occurred, which is likely to be a matter of crucial importance in the long run. Democratisation cannot be regarded as just a linear, one-way process, in any part of the world.

There are strong grounds for doubting that transitions from authoritarian into democratic regimes will prove sustainable unless they have established 'the social supports that usually only advanced economies can supply' (Crouch & Morley, 1998). The decisions of political actors may be crucial for determining the immediate direction and timing of regime changes, but they are made 'in a social context in which the level of economic development remains a fundamental element and one that is likely to have a serious impact on the sustainability of any changes made' (Crouch & Morley, 1998). In short, poor and crisis-prone countries are likely to have trouble maintaining democratic regimes, even if they are fortunate enough to achieve them, whereas more prosperous countries have better chances of doing so — provided they too have been fortunate enough to achieve them, which is not always the case.

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REVIEW ARTICLE

The 'Stolen Generations': A Report from Experience

Kenneth Maddock

*Colin Macleod, **Patrol in the Dreamtime**, Random House, Milsons Point, 1997*

COLIN MACLEOD'S unpretentious memoir recalls the lost Aboriginal world of the Northern Territory 40 years ago. It is not a world to which he looks back in anger, but neither does he see it through a rosy haze. From his second afternoon in Darwin, spent visiting native camps with Gordon Sweeney, a former missionary, he remembers

squalor and destitution: mangy dogs, dust everywhere, rubbish strewn across the camp, a couple of sticks slowly smouldering, the yabba yabba of what was to me aimless conversation, women dressed in dirty old cotton frocks, men in loincloths, kids with runny noses, flies in their eyes. There was no running water, no showers, no sewerage ... the people seemed bewildered. (p. 29)

Macleod had barely turned 21 when he left Melbourne for the Territory as a cadet patrol officer in the Welfare Branch. Until then he had known the secure tedium of clerking at the Williamstown Naval Dockyards, a stint of National Service, a mediocre record as a pupil in Catholic schools. More loftily, there had been a half aspiration to the priestly life, followed by fantasies about the Fleet Air Arm — how wonderful 'to swagger through the dockyard gates, rigged in a bright new Sub Lieutenant's blue uniform, gold wings embroidered above the gold ring on the sleeves' (p. 14).

He and his kind, the 'young blokes' who became patrol officers in the Territory or in New Guinea, wanted 'adventure and a change from the mundane' (p. 97). Saving the natives or doing altruistic social work were not on the agenda. As we follow Macleod through town camps, across vast pastoral properties, to government welfare settlements and Catholic missions, into the desert or out to the mouldering

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township of Borroloola in the Gulf country, we can guess that he got what he wanted. Yet it cannot have been enough, for within a few years of his arrival in 1955 he threw it away, becoming a full-time student of law at the University of Melbourne in 1959. Since then, however, while pursuing a career at the bar or on the bench, he has occasionally revisited the Territory, and so is able briefly to compare then with now.

No doubt it is convenient for governments that young men can always be found who crave after action and adventure in the open air. But if this is what the Welfare Branch could offer a patrol officer, there was a more serious point to its existence, which was to prepare Aborigines for assimilation into society at large. Part of the value of *Patrol in the Dreamtime* is that, in the unassuming form of a slice of one man's life, it throws light on what it was like doing spadework for an objective that many people are now quick to condemn. Macleod himself must have become completely disillusioned with the system, for in 1959, in an article for the Melbourne journal *Prospect*, he described the welfare settlements of the Territory as 'human zoos' (p. 229). Today he is less severe. Halfway houses were necessary, 'and so the settlements were probably as good as any other solution ... If there hadn't been a system holding back the thousands of natives that wanted to flock to the towns, Third World humpies and nightmare slums and exploitation by the white population would have been far worse' (p. 230).

Macleod was spurred into writing his memoir by irritation at the emotive and often uninformed debate over so-called 'stolen generations', the Aboriginal children removed from their families or mothers and either fostered out or put in such institutions as Sister Kate's in Perth, the board of management of which was once adorned by a lawyer named Ronald Wilson, who later became a judge of the High Court and later still lent his name to allegations of Australian genocide.

The 'Generation At Risk'

Sister Kate's is a good case to think about, because of the abyss which separates the views expressed when it was opened on 19 February 1972 and those that are now put forward about institutions of the kind. Professor W. E. H. Stanner, the most distinguished scholar of his day in the field of Aboriginal social anthropology, a man who was active and eloquent both publicly and behind the scenes in advancing what he took to be Aboriginal interests and in conveying to the population at large a subtle sense of what Aboriginal tradition meant to its inheritors, gave an opening address which is more fascinating to read today than it would have been to hear then.

Stanner began by conveying an apology from Dr ('Nugget') Coombs who was unavoidably absent. 'It would have meant a great deal to him — both as a West Australian and as a tireless worker for a better future for all the Aboriginal people — to be here to speak in his own way about his personal and official interest in ... Sister Kate's Children's Home. But it just could not be.' Nevertheless, Stanner hoped that Nugget would soon visit the Home to 'learn at first hand of the proposals for future developments', and that he would be accompanied by Barry Dexter, a leading public servant of the time, who with Stanner and Coombs formed the

Council of Aboriginal Affairs, a triumvirate of wise elders who gave top-level advice to the Commonwealth government.

If Stanner appreciated Sister Kate's endeavour, it was out of conviction 'that one of the oldest insights in Australian history is our perception that, if we could do anything at all for the Aborigines, our best hopes lay in doing it through their youths and children. I think that is still as true and valid as it ever was'. At Sister Kate's he could 'see for [him]self how ... at least some of these children are being given a prospect of a better life'.

A restless desire by the well-meaning to do something for what Stanner called 'the generation at risk', meaning Aboriginal children of school age or younger, runs like a thread through Australian history. It shows up in the eclectic and freethinking Phyllis Kaberry, an anthropologist contemporary with Stanner. During her field-work in 1934 at the Forrest River Mission in the Kimberleys, she became concerned at the plight of eleven half-caste girls in late adolescence. Because there were only two or three half-caste boys of a suitable age for them to marry and because 'of the absolute undesirability of marriage with a full-blood, the position of the remaining half-caste girls presents an extremely difficult problem. Perhaps one solution would be to send them to a half-caste mission such as Yarrabah in Queensland' (Kaberry, 1935:420).

Marie Reay, a generation later among anthropologists and an admirer of Stanner's, argued that policy should be sufficiently flexible for Aborigines 'to make their own choices without being brainwashed by do-gooders and petty officials' (Reay, 1964:xx). This was in *Aborigines Now*, her collection of essays by some Young Turks of the discipline. Neither the 'stealing' of children nor the commission of 'genocide' rated a mention. Nearly a quarter of a century later she did raise the former topic in a foreword for *Being Black*, a new collection which is really a latter-day version of her own book. Working decades earlier with Aborigines of mixed descent in eastern Australia, Reay had found a fear among women that children might 'be rounded up and taken away to an institution just because they were Aboriginal'. She comments that, although the removal of children occasionally happened, few of the women 'appreciated that by the 1940s the children who were institutionalised were those who were judged to be neglected, whether they were black or white'. Critical to a child's fate was whether it had a grandmother to demonstrate 'practical concern' as distinct from the 'sentimental concern' displayed by mothers: 'children who were taken away were those who had no grannies, were skinny and unkempt [unkempt?], wagged school, and subsisted on whatever they could scrounge from their various aunts' (Reay, 1988:ix).

Her publications show the strength of Reay's interest in Aboriginal women and family life. Her colleague and younger contemporary Diane Barwick had the same interest. I do not recall that either woman wrote of 'genocide' or did more than touch in passing on the 'theft' of children. There must be significance in their silence. Were they so obtuse and callous as to fail to see what was going on before their eyes? Or is it that today the past is being twisted by falsification, special pleading and anachronistic moralising?

The latter is the likely explanation. A telling consideration here is that the Australian Law Reform Commission, in a substantial report on Aboriginal customary law based on work carried out between 1977 and 1985, devoted a chapter to 'Aboriginal Child Custody, Fostering and Adoption', but did not suggest that the removal of children constituted genocide, even though it accepted that 'large numbers of Aboriginal children [had been] removed from their families and placed within non-Aboriginal families and in institutions' (1986: para. 351). In a brief discussion of the Convention on the Prevention and Punishment of the Crime of Genocide, the Commission noted that 'genocide is restricted to forms of physical destruction. It does not include even deliberate acts aimed at the assimilation of a minority group or what is sometimes referred to as "cultural genocide"' (para. 171).

It is at this point that one can turn back to Macleod, whose observations were of the Northern Territory. The government was removing part-Aboriginal children on welfare grounds in his time, though he says it was no longer happening to children of full blood. Memory has the power to disturb, but it does not lead Macleod into condemnation, for he considers the practice averted much worse befalling those subjected to it, who were more often girls than boys (for horrific examples of what they could suffer, see pp. 171 and 175-6). Noting that in the Darwin of the 1950s the Welfare Branch did get criticised for taking children, he asks:

But what if the mother was barely out of puberty, with no way of independently looking after herself, let alone her child? What if the mother was under the influence of some dissolute itinerant stockman? Young girls were becoming mothers way before they were old enough to be good mothers, in conditions of unspeakable squalor and cruelty, often inflicted by the child's father — if he had bothered to hang around — but more likely at the hands of those in the Aboriginal community who had no truck with 'yella fellas'. (p. 166)

Before me as I write I have an article by Rosemary O'Grady, a lawyer who cannot be numbered among Sir Ronald Wilson's admirers. She, too, has some questions, but hers are for the 1990s. How would a barrister advise 'a person who, a few years from now, seeks a remedy for child abuse now being suffered in [Aboriginal] communities?' Who sees to the rights of children when 'the authorities do nothing'? When 'welfare does get involved, the child is frequently "placed" back in the same household from which it has been, ostensibly, removed'. At a community in South Australia, 'wife-bashing, assaults and child abuse have sky-rocketed', while at another, owing to brawls among drinkers, 'It is impossible for anyone to sleep. It sounds at 2.30am like a war zone' (O'Grady, 1998:53-4).

O'Grady's cry from the heart, which reads like a depressing footnote to Macleod, might be criticised from the standpoint of conventional legal wisdom, according to which one should never get emotionally involved with a client, though in her case she has taken aboard the interests of an entire population. But in the light of Colin Tatz's relatively more detached survey of the state of Aboriginal communities

she cannot be dismissed as obviously overwrought. In 1989-90 Tatz surveyed 70 communities across the country, some of which he had known for decades. Among the 'realities for which there is, regrettably, abundant evidence' (1990:250), Tatz included (i) the great deal of personal violence within Aboriginal groups, even within families; (ii) the great deal of child neglect, as in hunger and lack of general care; and (iii) the considerable amount of violence and damage committed in sober states. He acknowledges that 'there is evidence from a number of scholars to show that [these realities] have a basis in tribal tradition', unlike other 'realities' which have arisen from culture contact. Tatz does not deal with child removals in his paper, but we can be sure that some of the situations he so candidly describes would have been seen by an old-fashioned public servant like Macleod as ones from which it could be justifiable to rescue children.

I arrived in the Territory for anthropological fieldwork in 1964, five years after Macleod left. In that year nearly all the legal disabilities to which Aborigines were subject in his time were repealed by the Social Welfare Ordinance. But because the new law came into effect only later in the year I was able to catch a glimpse of the restrictive regime he had helped administer. To a university intellectual for whom life was virtually synonymous with what the beautiful harbour cities of Auckland and Sydney had to offer, conditions in the Territory were harsh and Aboriginal affairs afflicted with a petty dullness. It would have seemed absurd, however, to impute evil to the regime, and I cannot recall anyone doing so, let alone suggesting that genocide was being or had been until recently practised under the guise of child welfare. My acquaintances included academics who travelled widely in the Territory to do research, some of whom, like the outspoken political scientist Tatz, the pre-historian Carmel White and the anthropologist John Bern, were of Jewish background and interested in Israel. That even they, to the best of my recollection, caught not a whiff of genocide throws into relief the hyperbolic excesses to which some latter-day commentators have succumbed.

Policy and Progress

No reader of Macleod's book is likely to finish it feeling that all was well in the 1950s. As he remarks, 'Even liberally-minded Europeans lived with assumptions we would today shudder at' (p. 70), though the example he gives to illustrate the point is so innocuous that it could cause only the most timorous to tremble. Comparing my memories of the 1960s with his, I am sure that in the intervening decade life had become freer, more hopeful and materially better for many Aborigines, perhaps for them all, but it would be churlish to deny that these were ends at which the Welfare Branch and the government of the day were aiming. I do not remember town camps like those he visited on his second day in Darwin; and the Beswick Reserve, where I did most of my research between 1964 and 1970, was a different place in my time. Whatever criticism one might make (on which see Maddock, 1977), the settlement there had ceased to be 'a haphazard assortment of lean to's [*sic*], humpies and huts constructed with bush timber and bark, cast-off materials such as hessian and rusted iron sheets, and the occasional piece of milled timber';

children were no longer 'regularly suffer[ing] from infected ears, and running noses and eyes'; and it would have been travesty to describe the food provided by the communal kitchen as 'terrible' or to characterise life in the camp as 'crowding, squalor and diseased dogs' (pp. 81-5). At a more general level it was inevitable that the extension of citizenship rights would curtail petty interference in people's lives, and likely that it would lead to land rights in some form.

Yet Tatz for one is a shaken man — with good reason, too, if he and O'Grady are drawing from life. Because the picture they give conflicts with my observations in the parts of Queensland, Western Australia and the Northern Territory which I have visited in admittedly random travels between 1978 and 1998, it is tempting, if unkind, to suspect that they are sensation-mongering. Unfortunately, as *Patrol in the Dreamtime* shows, it is not so simple.

In 1983 and 1995 Macleod revisited Melville and Bathurst Islands, which he knew well from earlier days, only to go away with a sense of decline and of lost vitality. 'There were no canoes in sight, no new grave poles, the gardens did not seem attended, and the sawmill was in ruins' (p. 136). It surprised him to find a 'large number of non-Aboriginals working there, compared to 1957, in spite of a supposed "independence" ... both islands boasted an Alcoholics Anonymous group and women's groups to help deal with domestic violence' (p. 228).

Some of Macleod's impressions are supported by the research of Eric Venbrux, a Dutch anthropologist who worked among the Tiwi on Melville and Bathurst Islands between 1988 and 1991. He found that homicide was occurring at ten times the United States rate. Because violence was even more common in pre-contact times, its modern level could not be blamed simply on Europeans. Rather, was it an effect, unforeseen and unintended, of the policy of self-determination adopted in the 1970s (Venbrux, 1995:16-17, 223-4). More recently, of course, Melville and Bathurst Islands have been in the news because of all the young men who kill themselves.

In spite of these gloomy indications I would not argue that Aboriginal communities are bringing about their own destruction, though there might be a stronger case for asserting it than for believing that they used to suffer genocide by child welfare. What is less doubtful is that many woes in Aboriginal life today spring from Aborigines themselves and from the policies that govern them. A wider recognition of this may come about if those involved in the Aboriginal affairs of our day report on their experience in the down-to-earth manner that Macleod has for his.

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NOTES AND TOPICS

The High Costs of Capital Taxation in Australia

W. Erwin Diewert and Denis A. Lawrence

THE important issue of capital taxation has been virtually ignored in the current Australian debate over tax reform. Discussion of alternative taxation options has been carried out in the virtual absence of comprehensive attempts to quantify the efficiency costs of different forms of taxation. Rather, the attention of business leaders, in particular, has been focused on the prospect of replacing the ramshackle wholesale sales tax with a relatively modest goods and services tax. While this is a step in the right direction, Australia needs to embrace much more fundamental reform of its taxation system, particularly as it relates to capital taxation. Australia's high capital taxes have reduced investment, lowered the size of the capital stock and impeded economic growth.

This note reports the results of the first steps towards creating a consistent analytical framework for analysing the efficiency costs of different taxes to the Australian economy. In particular, it provides initial estimates of the deadweight costs of capital taxation in Australia.

What Are Deadweight Costs?

In recent years there has been a growing focus internationally on the costs of raising taxation revenue. Communities have come to realise that, far from being free, rising government expenditure has to be financed sooner or later by increased taxation, and that taxation imposes a number of costs on the economy.

As well as the direct cost of the extra revenue and associated administrative and compliance costs, an important additional cost arises from the changes in behaviour induced by taxation. Taxes distort the incentives to work, save and invest, and the pattern of input use and production in the economy. These distortions impose costs on the economy by reallocating resources from their most productive uses to less productive ones. The losses created are known as *deadweight costs* or the *excess burden* of taxation. The deadweight cost of taxation is a measure of the value of the opportunities that are effectively lost when taxation diverts labour, land and

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capital from their best uses. By calculating the deadweight costs of taxation, we can gauge the potential effects of taxation on the economy and society and calculate the least costly combination of taxes.

The size of deadweight costs is influenced by a range of factors, but is likely to be largest when the actions of producers and consumers are highly responsive to after-tax prices, when existing marginal tax rates are high and when savings are highly responsive to after-tax returns.

Other Studies of Deadweight Costs

An earlier study by Diewert and Lawrence (1994, 1995) for New Zealand did much to raise the awareness of the deadweight costs of taxation among policy-makers and the general community. The key findings of the study were that the deadweight costs associated with labour taxation increased from 5 per cent to over 18 per cent in the 20 years up to 1991. Over the same period the marginal excess burden of consumption taxation (all indirect taxes other than property taxes and import duties) increased from 5 per cent to around 14 per cent.

However, while our first study made a number of advances in the measurement of deadweight costs, the estimates obtained are likely to be relatively conservative. By estimating a static model we were not able to calculate the marginal excess burden of capital taxation. Other studies which have attempted to introduce dynamics and model capital accumulation decisions have shown that the marginal excess burden of capital taxation is generally higher than that for labour given capital's far greater mobility. This is especially likely to be the case for small open economies such as Australia and New Zealand trading in a world of ever-increasing capital mobility and globalisation.

A few previous studies have attempted to estimate marginal excess burdens for Australia, notably those of Findlay and Jones (1982), Han (1996) and Campbell and Bond (1997). However, these studies all use static models and concentrate on labour and commodity taxation. While capital tax deadweight losses are likely to be far higher, studies that have successfully quantified them are rare, owing to the conceptual and implementation difficulties associated with building dynamic models. The work of Jorgenson and Yun (1991) in the United States is one important exception.

Tax Rates on Capital

In calculating the deadweight costs caused by taxation we need to know the size of the 'wedges' taxes impose between the price paid by the consumer or user and the price received by the producer or supplier. Tax rates on labour and capital returns are presented in Figure 1.¹

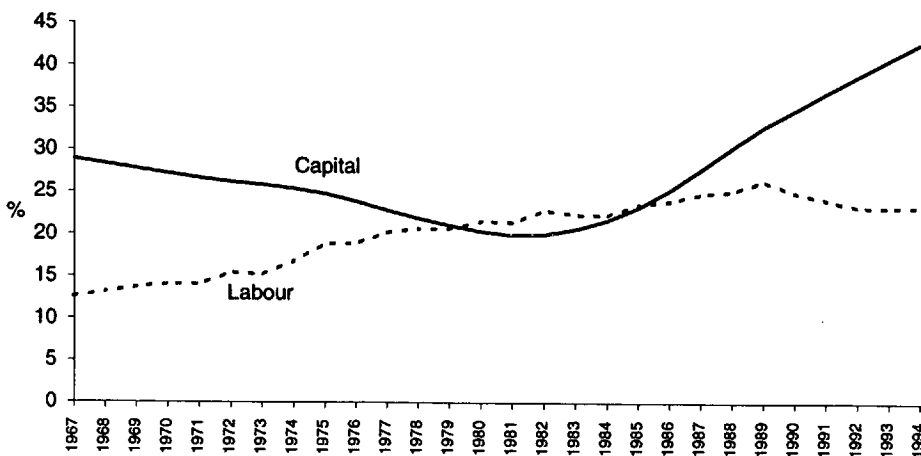
Changes to the Australian tax system since the mid-1980s have fallen relatively heavily on capital. The average tax rate on labour income increased over the 28-

¹ The database used in the study is described in Diewert and Lawrence (1997).

year period up to 1994 from 12.5 per cent in 1967 to 23.3 per cent in 1994. The labour tax rate peaked in 1989 at 26.4 per cent. After starting at 28.9 per cent, capital tax rates progressively declined to a rate of 19.9 per cent in 1981. Since then capital tax rates have again increased steadily, up to 42.7 per cent 1994. This increase in the overall rate of capital tax can be attributed to the introduction of capital gains taxes, increasing reliance on transactions taxes and the progressive tightening of exemptions from the tax base.

Figure 1

Labour and capital tax rates, 1967-94



Source: Diewert and Lawrence (1997).

Capital Tax Deadweight Costs Are High

Our estimated capital tax marginal excess burdens are presented in Figure 2. For each year, the marginal excess burden represents the incremental loss of net output divided by the incremental increase in tax revenue induced by an increase in the capital tax rate. The estimates are derived from an econometric model of the production sector described in the appendix to this paper and summarised in Diewert and Lawrence (1997).

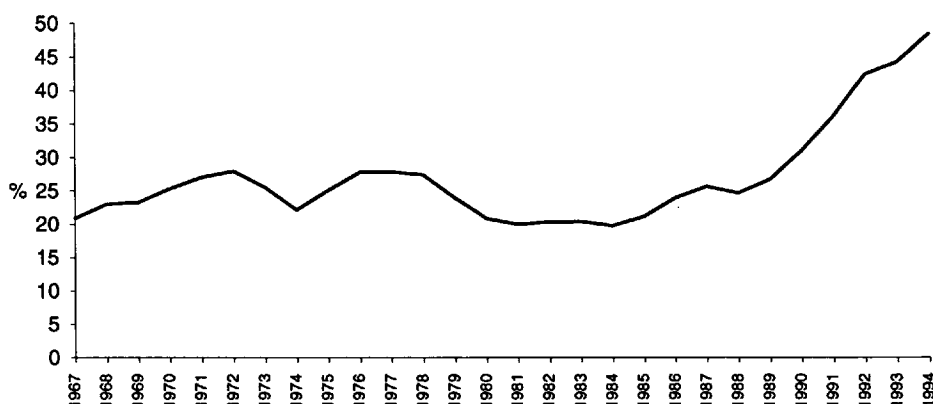
After starting from a figure of 21 per cent in 1967, the capital tax marginal excess burden climbed to a high of 28 per cent in the late 1970s. It then fell back to a low of 21 per cent again in 1983. Over the last decade, however, the capital tax marginal excess burden has climbed steadily to finish at a high of 48 per cent in 1994.

Policy Implications

What are the implications of these results? The essential implication is that, far from being free, government expenditure comes with a high price tag and must correspondingly be spent wisely on high-yielding projects or not at all. To be justified, a government project must not only provide the going return on the amount spent but must provide an additional return which covers the deadweight cost associated with raising that revenue.

Figure 2

Capital tax marginal excess burdens, 1967-94



Source: Diewert and Lawrence (1997).

The precise nature of the penalty this imposes on government projects depends on the nature of the project. There is an important difference between government expenditure on investments which provide a stream of returns over time and recurrent expenditure projects.

Consider first the case where the government raises an extra dollar of revenue from capital taxes and then invests this dollar in a perpetual project that earns $\$r$ in each period. In the following period the level of capital taxation returns to its old level but the government continues to receive the return from the dollar invested in the perpetual project. Let the discount rate be R . Then the discounted stream of benefits that the project earns (B) is:

$$(1) \quad B = r/R.$$

If we assume the deadweight cost associated with raising capital taxation is d then the above present value of benefits can be set equal to the current cost of $(1 + d)$ and we can solve for the ongoing return r that would be required for the project to

be worthwhile in view of the extra burden imposed by the increase in taxation. We obtain:

$$(2) \quad r = R(1 + d).$$

If we think of both r and R as being real returns (returns adjusted for inflation), then if $d = 0.48$ and $R = 0.05$, we must have $r = 0.05(1 + 0.48) = 0.074$. Under these assumptions, with a going real rate of return of 5 per cent, a perpetual project financed by increased capital taxation must earn a real rate of return of 7.4 per cent to be justified: an excess of 2.4 per cent over the going real rate of return.

However, while this is a major hurdle for an investment project, the penalty is far larger for a government project which involves recurrent expenditure. A recurrent expenditure project must provide a return each year which exceeds its direct cost (including a normal return) by at least the amount of the marginal excess burden. This is equivalent to earning an ongoing real rate of return over and above the normal rate of return by at least the estimated percentage of the marginal excess burden. This is because the return from the project occurs only in the year the expenditure is made, and to maintain an ongoing return the level of capital taxation has to be raised permanently.

For example, in 1994 a recurrent expenditure government project (such as a transfer payment) financed by additional capital taxation should have earned a real rate of return 48 percentage points above the normal real rate of return in order to overcome the adverse effects of increased capital taxation.

In 1994 the high cost of capital taxation can be alternatively illustrated by considering that a reduction in recurrent government expenditure financed by reduced capital taxes would have led to a real rate of return of 48 per cent. There are very few, if any, government projects which can boast such a high real rate of return.

It is important to note, however, that our study is not saying that less government spending is always better. The optimal level of government spending is not zero. The government has an important role to play, for example in providing public goods and physical and legal infrastructure that would not be supplied in desirable quantities through private transactions. It is worth incurring the marginal deadweight costs of taxation up to the point justified by the returns to such expenditure. Our study highlights the high opportunity cost of public funds and the need to spend those funds very carefully.

More important, these results indicate that by significantly reducing its capital tax rate Australia can remove some of the competitive disadvantage it faces compared to its low tax neighbours. The way to attract footloose, capital-intensive industries to Australia is not to give them selective incentives and to attempt to pick winners but rather to ensure that Australia's capital tax system is as competitive as possible across the board. Continuing globalisation and international economic integration means that Australia has to look at fundamental rebalancing of its tax

system to reduce the impost on its most internationally mobile factor, namely, capital.

Appendix: Methodology

There are many approaches to determining the efficiency costs of capital taxation. The approach we take is the following. We assume that the private production sector of the economy uses inputs of capital, labour and imports to produce consumption goods, exports, government purchases of goods and services and investment goods. We assume that investment goods produced in the current year are added to the capital stock at the beginning of the following year. Domestic households and foreign investors require interest payments in order to induce them to supply financial capital to the production sector.

We view the business income tax as falling on the return to capital, so that the rate of return that the private production sector must earn is increased by this capital tax. The effect of the capital tax will be to reduce the equilibrium level of capital, investment and domestic net product. In an equilibrium situation, investment goods are produced so as to just offset depreciation, and an optimal capital stock is one that maximises net output minus interest payments subject to primary resource constraints. Capital taxation moves the economy away from this optimal situation. Our approach to capital taxation is based on that developed by Diewert (1981:65-8; 1988:19-23).

The construction of the database used in this study largely follows the approach outlined in detail in the appendix to Diewert and Lawrence (1994), with the exception of the treatment of capital and investment goods. The principal data sources for this study are Australian Bureau of Statistics and Organisation of Economic Co-operation and Development (OECD) data contained in Econdata (1996). The database runs for 28 years from 1966-67 to 1993-94 and the market sector producer model estimated contains twelve goods. These comprise three variable outputs (general private consumption; government consumption of goods and services; and exports), two variable inputs (imports and labour), three investment goods (plant and equipment; non-residential and other construction; and inventories) and four capital stocks (plant and equipment; non-residential and other construction; inventories; and business and agricultural land).

The characteristics of the production technology are estimated using a variant of the semi-flexible normalised quadratic profit function with curvature imposed and incorporating splines on the technology variable.

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No Clear Objective: The Simons Report on Foreign Aid

Peter Warr

AUSTRALIA'S foreign aid programme currently costs taxpayers around \$1.5 billion a year, equivalent to about \$100 for each Australian. The recently released Simons Report, titled *One Clear Objective: Poverty Reduction through Sustainable Development* (Committee of Review on Australia's Foreign Aid, 1997), reviews the aid programme. It is a welcome and long overdue contribution to the formulation of Australia's policy in this important area. The Report contains much that is sensible and constructive and its recommendations are wide-ranging. They attempt to reformulate the principles guiding Australia's foreign aid. One of the Report's stated objectives is to stimulate a vigorous debate. In that it has succeeded and, in the spirit of that objective, I offer this contribution to the debate.

The Objectives of Aid

The predecessor to the Simons Report was the 1984 Jackson Report, which articulated three objectives for aid: humanitarian, diplomatic and commercial (Committee to Review the Australian Overseas Aid Program, 1984). The Simons Report recommends substituting the one objective of poverty reduction referred to in its title. I have three problems with this proposed change.

The 'one objective' is not clear. The Report does not define 'poverty reduction'. Some passages imply that it means alleviation of absolute economic hardship, while others suggest that it means reduction of relative inequality, sometimes also called 'relative poverty'. For example, the Report cites the World Bank estimate that between 800m and 1.3 billion people subsist on less than US\$1 a day, and then goes on to say that 'Massive inequalities are self reinforcing and destabilising' (p. 55). These two interpretations of 'poverty' are very different. Absolute poverty incidence and relative inequality are not the same thing; they do not necessarily move even in the same direction over time; and their economic determinants are quite different.

An illustration of the difference between these two concepts is provided by the recent experience of Thailand (see Warr, 1994). The Thai government's household survey data reveal that over the two decades since the mid-1970s relative inequality in Thailand increased, while absolute poverty fell. The share of total in-

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come received by the poorest one fifth of the Thai population fell from 6.1 to 3.8 per cent over the period 1975 to 1994. But this does not mean that the poor were worse off in absolute terms, because total Thai income per person more than doubled in real terms over the same period. The poorest one-fifth of the population (quintile) gained in absolute real income by around 50 per cent, even though the richest quintile gained proportionately three times as much, by around 150 per cent, again at constant prices. Over the same period, the incidence of absolute poverty, as measured by the proportion of the population whose incomes fell below a 'poverty threshold' level of income held fixed in real purchasing power over time, fell from 30 per cent of the population in 1975 to just under 10 per cent in 1994 (Bangkok Post, 1996).

Hardly anyone would say that the form of development Thailand experienced was ideal, but did it reduce poverty or increase it? The answer depends on what we mean by 'poverty', but the Simons Report is ambiguous about this central matter. If a foreign aid programme, or any other tool of policy, were to be built around the pursuit of a single objective, that objective would need to be made much clearer than it is in this Report.

In confusing absolute poverty with relative inequality, the Simons Report is not alone. The Australian Parliament's Joint Standing Committee on Foreign Affairs, Defence and Trade argued in 1996 that the government's newly established Committee of Review into Australia's aid programme (the Simons inquiry) should:

consider further the issue of the relationship between economic growth and the alleviation of poverty with specific reference to the dangers of polarisation of the rich and the poor. (Parliament of Australia, 1996:11)

This recommendation confuses the relationship between economic growth and relative inequality ('the polarisation of the rich and the poor') with the relationship between economic growth and the incidence of absolute economic hardship ('the alleviation of poverty'). They are not the same, and it is disappointing that the Simons Report confuses them again.

The Report says that:

Leading development organisations such as the World Bank and the United Nations Development Programme now agree that in addition to promoting growth in a broad sense, aid interventions need to be more carefully targeted to promote patterns of growth which maximise the impact on poverty. (p. 77)

For this to become more than rhetoric, we must begin by saying what we mean by 'poverty'; but that is only a beginning. Very little is currently known about the manner in which absolute poverty, relative inequality or any other specific conception of 'poverty' is affected by different forms of aid intervention. This is presumably why

most of what the Simons Report says about the way poverty is affected by different forms of aid, and different patterns of development, consists largely of platitudes.

The Report equally fails to define 'sustainable development'. In the development literature, the concept of sustainable development has been defined in so many contradictory ways that it has virtually no value as a tool of communication. As my colleague, Professor Ron Duncan, puts it, no one is against 'sustainable development' because it is a tautology: if development were not sustainable, it wouldn't be 'development'. But beyond that, no one seems to know what it means.

Why only one objective? Aid is a component of Australia's overall foreign policy. That policy has multiple objectives, more or less as described by the Jackson Report in 1984 (see p. 362 above). Ideally, each component of foreign policy should reflect those objectives. It is inefficient for any one component of foreign policy to be confined to the pursuit of only a single goal. From the point of view of the Australian taxpayer, it would seem reasonable to say that: (i) if foreign aid is to be constrained to the pursuit of only one objective it will then be a less efficient instrument for the pursuit of Australia's overall foreign policy objectives; and (ii) in that case, there should presumably be a lot less of it. That is, by unnecessarily restricting the objectives served by foreign aid, the recommendations of the Report threaten to undermine the constituency for it, and this is potentially self-defeating for the pursuit of the very goals the Report wishes to promote.

The Report is self-contradictory. Having insisted that poverty reduction through sustainable development should be the sole objective of Australia's aid, the Report then says this aid should be concentrated in the Asia-Pacific region. Why? The objective of poverty reduction at a global level might well be best served by concentrating all of Australia's assistance on, say, Somalia. The fact that almost no one would accept that extreme outcome, apparently including the Simons Committee members, reveals that 'poverty reduction' is not accepted as the sole function of foreign aid. It is only by appealing to objectives for aid other than poverty reduction, including Australia's diplomatic and trade policy goals, that the report's recommendations on the geographic focus of aid could be justified. But the central conceptual thrust of the report is the rejection of these objectives.

In its official response to the Simons Report, the Australian Agency for International Development (AusAID) accepted 'in principle' the recommendation that 'poverty reduction' should be the sole objective of Australia's aid, but modified this objective to read:

To advance Australia's national interest by assisting developing countries to reduce poverty and achieve sustainable development. (AusAID, 1997:16)

The role of the words 'advance Australia's national interest' becomes somewhat clearer from AusAID's response to the Simons recommendation that Australia's aid should be focused more tightly on the Asia-Pacific. AusAID accepts this 'in

principle' as well, but notes that 95 per cent of Australia's aid is already focused on 22 Asia-Pacific countries. It adds that

The Government will consider options for further tightening this focus but considers opportunities are limited taking into account Australia's interests. (AusAID, 1997:8)

What interests could these be but the diplomatic and trade objectives that the Simons Report recommends be disregarded?

The Fungibility of Aid

Like the Jackson Report before it, the Simons Report puts too much stress on the appropriate composition of aid. It overlooks the fact that aid is fungible.

Aid virtually always provides things that are substitutes, perfect or imperfect, for things the government of the recipient country is *already providing* through its own resources. When aid provides, say, more hospitals, the recipient country's government quite rightly takes that aid into account in determining the subsequent allocation of its own budget. It will reduce the expenditure on hospitals that it would otherwise have made, and spend more on, say, schools and defence equipment. The net outcome of the aid is that citizens of the recipient country end up with more hospitals than they would have had otherwise, but not as much more as the composition of the aid itself may suggest. They also end up with more schools and defence equipment. If the aid had consisted entirely of schools or defence equipment, the net outcome would have been approximately the same. When the aid provides things that are only imperfect substitutes for the government's own expenditures, this argument is weakened, but only slightly.

It follows that aid donors are deluding themselves if they believe that the composition of their aid determines its net effect on the goods and services finally delivered to citizens of the recipient country. The efforts of donors in that respect are largely undone by the adjustment of the recipient government's own budgetary allocations, in the light of its own objectives. The net effect of aid therefore depends primarily on just two factors: the volume of aid and the preferences of the recipient government. The final impact of the aid is therefore roughly the same as it would be if the recipient country were given money to spend as it pleased.

To the extent that we are concerned about the impact that aid has on the people of the recipient country, there are just two questions to ask. Do we want to give aid to a particular country, taking account of the policies of its government, and if so, how much? The aid might as well be given in money, but if we are required to donate in kind then the sole question to ask about the composition of that aid is: what form(s) of aid can we deliver most efficiently?

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Does Compulsory Voting Distort Electoral Outcomes?

Gary Johns

IS compulsory voting 'the great guarantee of truly democratic elections' that Neville Wran (1997:1) believes it is, or should the obligation to vote be converted into a right to vote or not to vote? This challenge is now upon the electorate following the recommendation by the Parliamentary Joint Standing Committee on Electoral Matters (1997:xx) that Section 245 of the Commonwealth Electoral Act, which provides for compulsory voting, be repealed.

Australians do in fact have the right not to vote, but few know it. A voter is not obliged to cast a vote by marking the ballot paper, and can comply with the law merely by returning the ballot to the ballot box. Although this latter claim is open to debate (Twomey, 1996:209), the secret ballot makes detection of an unmarked ballot difficult, if not illegal, and thus ensures that voters need not vote. However, the advertising accompanying the election for the Commonwealth parliament, and the emphasis on making a formal vote, give voters the strong impression that it is compulsory to vote. Indeed, more than 95 per cent of Australians do vote on a regular basis, and have been doing so since the 1925 election (Parliamentary Research Service, 1994/95:85).

The cost to the individual of compulsory voting is small, certainly when compared with, for example, that of compulsory jury service. There appear to be few signs of civil disobedience associated with compulsion; and compulsory voting appears to be popular: 74 per cent of all candidates at the 1996 Commonwealth election favoured compulsion (Jones et al., 1996:40), as did 70 per cent of the electorate (Mackerras & McAllister, 1996:Figure 1).

Debate about compulsory voting tends to concentrate on the moral issue of whether voting should be obligatory (Jones, 1996) or a right that one may choose not to exercise (Minchin, 1996). Yet both supporters and opponents of compulsory voting are also concerned about a number of issues that are open to empirical and theoretical investigation. They are concerned about three issues in particular: the level of voter turnout; any bias in the vote associated with a given turnout; and any impairment directly associated with either compulsory or voluntary voting. This note explores these issues and tries to come to some conclusions about them.

Voter Turnout under Voluntary Voting

In response to a report that 88 per cent of Australians would vote if voluntary, Senator Nick Minchin, the Liberal Party's main advocate of voluntary voting, stated that he was delighted 'that such an overwhelming majority of Australians would freely choose to exercise their right to vote without being forced to do so by law. Nothing could better demonstrate how unnecessary compulsory voting is...' (quoted in Jackman, 1997:1). The assumption is that a higher turnout is preferable to a lower turnout.

If compulsory voting were abolished in Australia, it is generally agreed that turnout would drop. But by how much? Would it be nearer the 59.2 per cent turnout of eligible voters in the 1922 Commonwealth election that sparked the legislative introduction of compulsion in the first place, or the 88.3 per cent voluntary turnout in New Zealand in 1996 (Mackerras & Smiley, 1997:632)?

The voluntary postal ballot for the 1998 Constitutional Convention in Australia recorded a turnout of just under 47 per cent. This figure is probably lower than it would be for a Commonwealth parliamentary election, which voters may take more seriously, although the requirement that voters attend a polling booth in order to cast a ballot is more time-consuming and may dissuade even more potential voters under a voluntary vote than the postal version. Nevertheless, the experiment suggests that a substantially lower turnout could be expected under a voluntary ballot. Jackman (1997:42) estimates, based on non-response and estimation of measurement errors of Australian survey data, that with the abolition of compulsion 'substantially lower rates of voluntary turnout would eventuate, perhaps as low as those countries like Japan or the US, in the 50 per cent to 60 per cent range'.

A change of voting law in Austria for its 1986 federal election fortuitously made possible a comparison of turnout in the Austrian province of Carinthia, which introduced mandatory voting for the election, and in surrounding provinces which remained voluntary. With a turnout of 92 per cent before the change to the law, Carinthia was already an highly participatory electorate. Even so, the rate jumped by 2.2 percentage points, and by 5 per cent relative to other provinces (Hirczy, 1994:74). This study suggests that the abolition of compulsion, in the first instance at least, would lead to a fall in turnout even where there was a political culture of high turnout.

Turnout and Bias

In what ways, if at all, is democracy harmed by a low turnout?

Compulsion and information. It is a reasonable assumption that any loss of information is detrimental to democracy. Democracy reflects the information that citizens have about politics, sufficient at least to allow them to vote, whether in their own self-interest or for the common good. But, as Lau and Redlawsk (1997:585) remind us, only a tiny minority of citizens live up to the ideal of participation that democratic theorists like J.-J. Rousseau and J. S. Mill recommended. Other com-

mentators argue that political indifference is a good thing, since it promotes stability by dampening the impact of the ideologues. Presumably this means that the ignorant and the indifferent have to express those 'views' by voting, and that to this end it can be held that 'compulsory voting affects political culture in a conservative way' (Parish, 1992:18).

In a study of voters in the US, where voting is voluntary, Lau and Redlawsk (1997:586) found that a surprisingly high 75 per cent of voters voted 'correctly', in the sense that the votes they cast were 'the same as the choice which would have been made under conditions of full information'. Would the percentage of 'incorrect' votes be even higher under compulsion? The study cannot tell us, but it does suggest a probable loss of 'correct' votes among those who do not vote: that is, a loss of valuable information from the democratic process.

Partisan bias. Mackerras and McAllister (1996) suggest that compulsory voting has a built-in bias against right-wing parties and in favour of left-wing and minor parties. In Australia, support for compulsion by the ALP, the Australian Democrats and the Greens suggests that this is indeed the case. But this is surely just the obverse of the bias against left-wing parties that would follow an abolition of compulsion. McAllister (1986:92) has estimated that, if turnout fell to 1922 proportions, Labor would lose nearly 4 per cent and the Liberals would gain 2 per cent on the 1977 election result. For the 1996 result, Jackman (1997:40) concludes that, 'as turnout diminished, the Liberals' share of the vote could be as much as 7.4 percentage points higher than the ALP's'.

The vote that the ALP receives as a result of compulsion could be viewed as an error that voluntary voting would avoid. But it should more accurately be viewed as valid opinion that would otherwise go unmeasured. Only the complete population supplies the accurate picture of the electorate's view; any move that would lower the turnout would almost certainly provide a biased sample of the voters' wishes. A return to voluntary voting thus risks a loss of collective judgment.

Does Compulsion Impair the Vote?

One measure of impairment associated with compulsory voting is the level of informal voting, which in Australia is high by international standards. However, it is generally accepted that this is the result of the interaction between compulsory voting, the complexities of the electoral system like preferential voting and differences in the voting rules for different elections, and the presence of a large number of non-English speaking migrants (McAllister, 1993:23). At the 1996 Commonwealth election, 3 per cent of the votes cast were informal; compulsory voting may account for a part of that figure, but even if it accounted for all of it, it hardly compares with a potential (and arguable) 30 per cent impairment to the vote under voluntary voting, if that proportion chose not to vote.

There are at least two important theoretical considerations. Shapiro (1990:112) desires to achieve a 'thoroughgoing pluralism of dispersed preferences'. Democracy as majority rule was originally an 'oppositional' ideal, an instrument for oppos-

ing the elite. In the Australian context, that elite could arguably be defined as an intelligentsia that exercises an undue influence on democratic politics. Such a tendency would be enhanced if less articulate citizens failed to vote. Democracy as an oppositional mechanism should be at its most powerful when the greatest number of potential non-voters vote, that is, when the dispersal of preferences is at its greatest.

Brennan and Lomasky (1993:225) advance a principle of 'responsible civic conduct' that could be interpreted as favouring compulsion. Their arguments opposing the secret ballot are also relevant. They claim that the secret ballot inhibits a culture of open discussion and leads to a monopoly of discussion by parties and journalists; only an open ballot can filter out anti-social voting motives like flippancy or meanness.² They imply that the suffrage should be restricted to those who 'have on hand an array of publicly acceptable reasons to justify one's actions' (Brennan & Lomasky, 1993:219). But if only such people voted, the likely loss of 'correct' votes would be high. As well, it is often the least articulate who are prone not to vote (McAllister 1986:91), but their contribution as an oppositional force can provide for a more thoroughgoing pluralism and in that sense encourages responsible civil conduct.

The one element of compulsion that does bear repeal is the exhaustive preferential ballot, which in effect forces voters to make a choice between the major parties. Rydon (1997:177) has suggested that the low turnout at the 1922 election may have been caused by a change from first-past-the-post to preferential voting, which some voters found difficult or objected to. In a sense, complexity begat compulsion. The proponents of the repeal of compulsion, however, have no intention of ditching the exhaustive preferential vote (there was no dissent on the issue in the Joint Standing Committee Report).

Preferential voting is a reasonable system, ensuring that the least number of votes are wasted (Taylor & Johnston, 1979:50). However, in 1996 Albert Langer drew attention to the fact that it was possible to cast a formal vote that avoided a choice between the major parties, since, under s.270 of the Commonwealth Electoral Act, a vote is formal even when a preference number is repeated and a box left unfilled. Yet Langer was gaoled because he committed the offence of advocating voting in a way that did not accord with the instructions on the ballot paper. This drives compulsion to the extreme, and increases the risk of an 'incorrect' vote being cast (one not reflecting the voter's opinion). There is a vast distinction between a system of compulsory voting where voters are required only to deposit a ballot in the box, and one where they are compelled to allocate preferences to all candidates. As Twomey (1996:201) has argued, where voters are compelled to express a preference for certain candidates they do not wish to, they are in effect being forced to lie.

The Joint Standing Committee recommended closing the 'Langer loophole', but only because it exploited a contradiction in the voting instructions in the Act,

²

It could be as forcefully argued that the secret ballot protects the voters from interference in casting their votes: which is, of course, why it was introduced.

which allowed for more than one method of casting a formal vote. If the recommendation for the repeal of compulsory voting had been accompanied by a recommendation for substituting compulsory exhaustive preferential voting with optional preferential voting, it might have been more credible. As it is, it looks like an exercise in partisan politics.

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REVIEWS

Defusing the Age Pension Time Bomb

Michael Littlewood, Will You Still Need Me? A Retirement Income Primer for Politicians, Employers and Meddlers, Planit Services Ltd, Auckland, 1997

Michael Littlewood, Will You Still Need Me? Retirement-Income Lessons from New Zealand, The IEA Health and Welfare Unit, Institute of Economic Affairs, London, 1998

Reviewed by Michael James

IN September 1997, New Zealanders voting in a referendum rejected by a huge margin a proposed Retirement Saving Scheme, a compulsory, funded and private income-retirement arrangement designed eventually to replace the country's generous pay-as-you-go national superannuation scheme. Michael Littlewood was a leading advocate of the 'no' vote. In his book (of which the British edition is essentially an abridged version) he puts forward a programme for converting New Zealand Superannuation (NZS) into an Australian-style means-tested safety net, while shifting working people's saving efforts very largely into private, funded but voluntary pension schemes.

From 1988 to 1997, Littlewood was employee benefits director for Fletcher Challenge Limited (New Zealand's largest employer) and in 1991-92 a member of the New Zealand government's Task Force on Private Provision for Retirement. In the former job he evidently learned how to explain the fundamentals and the details of retirement income in plain, even colloquial, English. This is one of his book's greatest strengths. Another is its comprehensiveness: all the main aspects of the subject are covered, including the operation of the private saving industry and how it could expand in response to reform of NZS.

New Zealand's retirement income policy in recent decades has differed significantly from Australia's. The Labour government elected in 1972 attempted to set up a compulsory superannuation scheme; the National Party won the following election after promising to replace it with a greatly expanded state pension. The Muldoon Government's scheme, introduced in 1977, amounted to a one-off transfer to retired and older workers at the expense of younger ones that contributed to New Zealand's economic decline in the 1980s. Since 1979, governments have been trying to get the scheme under control, but with only mixed success: a tax surcharge imposed on the highest-income retirees in 1985 was abolished (with the acquiescence of all political parties) in April 1998, a substantial victory for 'grey power' in New Zealand. But pressure for reform will continue: without it, the cost of NZS is

expected to rise from 4.5 per cent of GDP today to about 10 per cent in 2040. Sooner or later, Michael Littlewood's proposals will have to be taken seriously.

New Zealand's private saving policy regime, in contrast, is superior to Australia's. Littlewood approves of the changes in the late 1980s that restored tax liability for contributions to, and earnings of, pension funds, and exempted from tax the benefits they paid; he argues that tax incentives for private saving are distorting and, as they do not turn out to be self-financing, they increase overall tax rates. Littlewood also effectively demolishes the case for compulsory private saving. Even schemes that avoid the peculiar complexities and associated costs of Australia's superannuation guarantee inevitably suffer from two major problems. The first is the moral hazard induced by the government guarantees (implicit or explicit) that unavoidably accompany compulsion. This is bound to lead to underperformance. As evidence for this, Littlewood cites the Savings and Loan debacle in the United States in the 1980s, which he attributes to the deposit insurance that government provided for small savers. The second problem is the ability of people to find ways around compulsion so as to restore their natural saving preferences. As well as reducing saving in other vehicles (such as housing), they can borrow back excess saving (Littlewood cites evidence that, as at March 1996, Australians had borrowed the equivalent of nearly 90 per cent of their after-tax income, up from 70 per cent ten years earlier) and in the last resort join the black economy. The upshot is that compulsory schemes are unlikely to increase private saving and could even reduce it.

This brings attention back to the state pension. Compulsory superannuation is often defended as itself a solution to the moral hazard that consists of the temptation not to save enough for retirement in order thereby to qualify for welfare state benefits. But, as Littlewood observes (p. 146), a sufficiently modest and strictly targeted state pension would itself counteract such moral hazard by signalling that only private saving could guarantee a materially comfortable retirement. The core of Littlewood's book is a set of proposed reforms for NZS. He aims for a level of benefits somewhat in excess of what is sufficient to prevent poverty, and suggests 55 per cent of the net average wage for a married couple and 35 per cent for a single person: a drop of around 20 per cent from present NZS levels. As this level is still quite generous and considerably above the unemployment benefit, Littlewood pushes the burden of fiscal restraint on to other reforms. These include a universal eligibility age of 68 from 2014 (beyond the present gradual rise to 65 by 2001) with (from 1999) the option of taking a reduced benefit from age 60 or a larger benefit if taken after age 68.

The most important proposed reform is a means test. To counteract some of the incentive to rearrange one's affairs artificially so as to pass the test, Littlewood recommends two devices used in Australia: allowing a 'free zone' of private income and, in respect of any income beyond that zone, offsetting the pension by less than 100 per cent. He rejects the assets test as self-defeatingly complicated, and suggests instead an extended income test that applies to the underlying returns on a wide range of assets. To provide credibility and stability to his reforms, Littlewood pro-

poses delegating responsibility for monitoring the state pension to a statutory body known as the 'Retirement Trustees', an idea which, as Littlewood notes, resembles New Zealand's Reserve Bank Act 1989 in insulating an area of policy from short-term political pressures while ensuring the responsibility and accountability of the policy-makers. All the reforms other than those affecting age of eligibility would be introduced in 2045, so that the saving plans of people aged 20 years or more would not be disturbed.

These reforms go in the right direction, but do they go far enough? The proposed level of the pension is probably too high to discourage serious effort to circumvent the means test. Littlewood admits that 'there's no real science' (p. 183) in his suggestion, and he offers no fiscal scenarios for the various options; but pitching the level no higher than some notional poverty-alleviating level would create a stronger incentive to save privately and reduce the gains from trying to get round the means test. A body of Retirement Trustees could be captured by the grey power lobby unless its aims were spelt out as narrowly and clearly as is the Reserve Bank's job of keeping inflation low. Postponing the benefit cut and the means test for 47 years weakens the credibility of the whole programme by exposing it to the prolonged risk of being undermined by political opportunism. The reforms could surely start earlier; for example, since the pension was targeted through the tax surcharge for 13 years after 1985, some sort of means-testing could be resumed within a few years without any violation of legitimate expectations. The pension expectations of younger working people will have started to fall well before 2045, by which time an unreformed NZS would have come under severe pressure from other claims on the public purse.

Littlewood has done a very good job of exploring the main issues raised by retirement income policy and identifying the aspects of it that will have to be addressed. It's unfortunate that the presentation of the book doesn't match its contents. Despite its plain and lively English, it is less accessible than it could have been. At 388 pages, it is too long (though partly because of poor formatting). The references are not usefully listed at the back but are scattered throughout the many footnotes and in many cases are incomplete. Worst of all, there is no index, or even a detailed list of contents. The author tells us he published the book himself; he may have been rushing to bring it out before the September 1997 referendum. But, with a subject as large and complicated as retirement income, many readers would want to explore particular topics rather than read the book straight through. They would be well advised to consult the British edition published by the Institute of Economic Affairs, which contains an index.

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Commercialising New Zealand's National Television

*Barry Spicer, Michael Powell and David Emanuel, The Remaking of Television
New Zealand 1984 – 1992, Auckland University Press, Auckland, 1996*

Reviewed by Franco Papandrea

OVER the past two decades governments around the world have increasingly embraced microeconomic reform and privatised public-sector enterprises in pursuit of improved economic efficiency and competitiveness. Nowhere, perhaps, has this movement been promoted with greater zeal and sense of urgency than in New Zealand, where successive governments have vigorously sought to dismantle regulatory regimes and establish competitive markets for services traditionally delivered by government monopolies. In this book, three management academics at the University of Auckland give an account of the transformation of Television New Zealand (TVNZ) from a division of the Broadcasting Corporation of New Zealand (BCNZ) into a commercialised state-owned enterprise (SOE) operating in a competitive market.

The authors seek 'to examine the organisational and management process' (p. 3) of the transformation of TVNZ. They present the events and internal upheavals generated by the transformation process in a documentary style, relying mainly on interviews with key participants. They offer little by way of analytical assessment or comment; and the end product is much like a typical management-school case study of organisational change. Readers are left to make their own judgment on whether the strategies that were adopted were appropriate or whether different strategies might have been more suitable in the circumstances. Perhaps this was intentional and anticipated the likely use of the book as material for classroom discussion by students in the authors' own faculty and in other business and management faculties. The authors have certainly produced an excellent case study of organisational change that should appeal to management academics.

The authors' exclusive focus on organisational and management changes occasionally inhibits or overlooks simple explanations of, or insights into, actions that could have been understood with a more encompassing outlook. For example, phenomena such as look-alike programming on two channels both owned by BCNZ would not then have seemed puzzling. Underlying incentives and expectations from programme-choice models predict that advertiser-financed broadcasters owning multiple channels will produce complementary rather than competitive programming. However, in BCNZ common ownership was overlaid by separate organisational groups, each with its own director-general and without overall coordination. So the two channels behaved as competitors. As Hotelling (1929) demonstrated long ago, the underlying incentives for competitors in such a situation lead to the supply of similar programmes with broad appeal. Removal of competition by reintegration of the two channels changes the incentives in favour of complementary programming. Thus, a welfare-maximising broadcaster controlling multiple chan-

nels has no incentive to provide more than one service in the same sector of the market. Consequently, the realignment of the programming on the two TVNZ channels is likely to have been more a response to the reintegration of the two channels than a strategic response to anticipated competition from a new entrant.

The central and most fascinating part of the book discusses three distinct phases of the transformation process. The first phase is concerned with emerging pressures in the mid- to late 1980s, culminating in the Rennie Committee review's recommendation that the broadcasting functions of BCNZ be restructured into two SOEs, one each for radio and television. The second phase deals with the implementation of the Rennie's Committee's recommendation focusing on the establishment of TVNZ as an SOE. All of this occurred in the short period from August to December 1988. The third phase covers the period 1989-1992 and is concerned with the changes within the newly established TVNZ and the implementation of competitive strategies to limit the impact of the entry of TV3 in November 1989 and secure new business opportunities.

These chapters provide a very interesting and informative insight into a government organisation that had grown out of touch with the needs and desires of the community it purportedly served. The BCNZ, as here described, was an overly bureaucratic and overstaffed organisation lacking the motivation to pursue the necessary changes to deal with the challenges of an increasingly competitive environment. It had no clear direction or vision and was embroiled in a mishmash of commercial, bureaucratic, cultural and political issues. Its programming was driven more by the desires of producers than by audience demands or commercial realities. In the view of its chairman, it was 'seriously at risk of being swamped by waves of new technology and competitors surging into broadcasting' (p. 24). Then, in 1986, Julian Mounter was appointed Director General of television within BCNZ, and later became Chief Executive of TVNZ. Strongly convinced that rapid change was necessary for TVNZ's survival, he single-mindedly set himself to bring it about. There followed an excellent demonstration of the strategies and drive necessary to transform a moribund organisation opposed to change into a vibrant and competitive organisation that thrives on change.

Mounter's management style and actions betray more than a hint of guidance from the writings of Macchiavelli. In his early 16th-century classic *The Prince*, Macchiavelli (1961:51) advises:

It should be borne in mind that there is nothing more difficult to arrange, more doubtful of success, and more dangerous to carry through than initiating changes in a state's constitution. The innovator makes enemies of all those who prospered under the old order, and only lukewarm support is forthcoming from those who would prosper under the new. ... In consequence, whenever those who oppose the changes can do so, they attack vigorously, and the defence made by the others is only lukewarm.

Machiavelli's favoured solution to such a problem was to replace some key managers with new ones of the innovator's own choice, thus ensuring their support as well as giving a strong message to the retained managers that resistance would not be tolerated. This is almost exactly what Mounter did:

In the first year and a bit, I changed over 50 senior management jobs. A lot went out of the organisation. I gave them plenty of time, but they resisted, they argued, they wouldn't have it. ... I brought something like 20 Kiwis (from abroad) ... back into senior management positions. And I hired Kiwis here and promoted from within. This allowed us to rapidly build a team that agreed that there had to be a change. (p. 29)

The active strategies set in place to deny TV3 the means of establishing a substantial foothold in the market would be a useful guide to other organisations facing a similar threat. The two-pronged approach adopted was simple yet effective. First, action was taken to ensure that all major sources of popular programming were tied up in long-term supply contracts, thus denying TV3 access to them. Second, TVNZ's managers were asked to concentrate efforts on working out what strategies they would adopt if they were running TV3. This was done for every significant area of operation. The simulated strategies were then analysed to identify any weaknesses that needed to be addressed within TVNZ if the strategies were to be countered. This approach was spectacularly successful and largely responsible for TV3 going into receivership within six months of entering the market.

Although the focus of the book is on the changes facing TVNZ, the lessons it presents are likely to be applicable to other organisations undergoing similar changes. Indeed, it is unlikely that other situations would be as complex as the television case, where economic imperatives were overlaid with an intricate mix of political and cultural objectives that compounded the difficulties of the transformation process. Consequently, not only those with an interest in television but also those interested in the process of privatising government enterprises should find the book attractive and appealing.

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The End of Cohesion?

Organisation for Economic Cooperation and Development, Societal Cohesion and the Globalising Economy: What Does the Future Hold?, Paris, 1997

Francis Fukuyama, The End of Order, Centre for Post-Collectivist Studies, Social Market Foundation, London, 1997

Reviewed by Winton Bates

THE OECD publication *Societal Cohesion and the Globalising Economy* is based on papers presented at a conference held in December 1996 to 'stimulate innovative thinking about ways to maintain future societal cohesion in the face of a dynamic economy that thrives on a high degree of flexibility'. This raises the question of why a dynamic OECD economy that thrives on a high degree of flexibility would have any difficulty in maintaining societal cohesion.

Robert Lawrence (Harvard University) paints scenarios of the likely relationship between economic growth prospects and social outcomes over the next 15 years. The scenario he considers most likely, 'the doldrums', is a continuation of slow economic growth in OECD countries. He argues that 'while this may not be an explosive scenario, there are several elements in it that are disquieting' (p. 34). The plight of the poorest Americans would be likely to worsen as a result of a reduction in welfare benefits. Europe would continue to experience high unemployment. Japan's institutions would also begin to come under pressure, with lay-offs more common and diminished opportunities for young educated workers. Lawrence further argues that future growth rates will depend largely on the gains from technology and globalisation. He paints a rosy picture of the 'cyber-euphoria' likely to result if pay-offs in these areas are beyond current expectations, and a dismal picture of worsening social problems, including increased racial tensions, that are likely if the new technologies create disruption and dislocation.

In contrast to the technological determinism of Robert Lawrence, Henry Lepage (Institut Euro 92) argues that economic policy reforms that have eliminated inflation in many countries and put their governments 'on a diet' provide grounds for optimism. His vision for the next two decades is of a world of higher productivity gains. He suggests that, although income distribution will be unequal, this issue will become relatively unimportant because people will again be able to plan safely for the long term and provide for their own futures. He also suggests that there will be a return to the values of a society founded on the rule of law and individual rights.

Two other contributors present opposing views on the role of government in providing income security. Claus Offe (Humboldt University of Berlin) argues for provision of 'basic income' as a 'citizenship right'. What he has in mind involves paying people not to seek work (in order to offset the effects of labour-saving technical change) rather than attempting to minimise work disincentives.

Dennis Snower (University of London) views welfare programmes that have become the basis for 'an unemployed way of life' as a potential source of problems in achieving both prosperity and social cohesion. He believes that the welfare state cannot be relied upon to provide security:

In retrospect it can be seen that, just as many of the common OECD policy systems amplified the favourable social and economic developments of the 1950s and 60s, so they are amplifying the unfavourable developments that have occurred since then. This could be called the 'quicksand effect'. It signifies that, in the long run, the prevailing policy systems have not provided firm foundations for supporting people against poverty and uncertainty and promoting prosperity and social cohesion. Rather, the more people need to be supported, the greater are the political and economic pressures on governments to reduce that support. The prevailing systems, in other words, are a bit like quicksand: they start giving way as soon as enough weight is placed on them. (p. 42)

Snower suggests that social safety nets should be modified to provide beneficiaries with 'greater economic incentives to overcome the contingency' (p. 43) for which this social insurance is being provided. It is arguable that some OECD countries, including Australia, are making important steps in this direction.

The OECD Secretariat's overview (by Wolfgang Michalski, Riel Miller and Barrie Stevens) does take a clear position on the need for reform of the welfare state. The theme of the overview, reflecting the original objectives of the conference, is the perceived need for 'balance' between economic flexibility and societal cohesion. The authors acknowledge that competition and structural change are 'a motor of the economic growth and prosperity on which cohesion can thrive' (p. 7). However, they accept without question the view that the welfare state is 'central to providing citizens with a sense of security and reason to be committed to the society in which they live' (p. 13). They also argue that a policy of promoting flexibility by reducing the role of government would need to deliver 'considerable prosperity' if it was 'to gain the widespread commitment upon which societal cohesion depends' (p. 16).

When large numbers of people have become dependent on the state to provide them with income, it is obvious that many will be displeased if taxpayers vote to withdraw their support. It seems to me, however, that this provides a strong case for reducing the burden that the welfare state imposes on taxpayers before unrealistic notions of 'entitlement' become more deeply embedded in the quicksand. It seems reasonable to expect that those OECD countries in which a relatively high proportion of the population depends for income on the redistribution activities of government (rather than on mutually beneficial transactions with other citizens) will tend to have the greatest difficulty in coming decades in maintaining widespread commitment of their citizens to basic institutions.

Francis Fukuyama, famed author of *The End of History and the Last Man*, approaches the issue of societal cohesion from a different perspective. Whereas the main focus of the OECD volume is on income distribution and redistribution policies, the main focus of *The End of Order* is on family breakdown. Fukuyama describes the decline in the nuclear family that has occurred during 1965-95 in most OECD countries as 'the great disruption', and cites impressive evidence that the decline of the nuclear family and the absence of paternal influence over many young males has been responsible for a sharp increase in violent crime. He associates the decline of the nuclear family with the decline of the social norm of male responsibility, under which men accept responsibility for the consequences of their sexual activities: by marrying, and devoting a substantial part of their lifetime earnings to support of their wives and children.

What are the causes of this 'great disruption'? Fukuyama considers a range of factors, but settles on 'birth control and working women' (p. 45) as the main causes. He argues that with women able to take the 'pill' and to support themselves and their children, many men have felt liberated from norms requiring them to look after their sexual partners who got pregnant. This theory appears to fit the facts as to why the 'great disruption' occurred when it did and why it has not yet occurred, for example, in Japan. It seems to me, however, that the theory is not entirely adequate because it does not take account of the fact that, rather than being supported by working women, many single-parent families are supported by welfare payments.

The important question is what, if anything, can be done about social problems associated with the 'great disruption'. While Fukuyama does not see the welfare state as the cause of these problems, he certainly recognises that it does not provide a solution: 'even if it were affordable, it is not clear that the state can adequately perform the socialisation functions traditionally played by other, smaller-scale social groups and without hastening the demise of those very groups' (p. 121).

Fukuyama concludes with the thought that a religious revival might rectify the situation. He refers to historical precedents, including the role of the Wesleyan movement in the 19th century. Perhaps something similar could happen again, or, alternatively, large numbers of taxpayers might just decide that they are tired of picking up the bills for irresponsible behaviour by others. This could be sufficient to initiate public policy reforms which, as Fukuyama acknowledges, could help restore to males an incentive to take responsibility for their children. A good place to start in thinking about this is the proposal by David Green (1996) that fathers who neither marry the mother of their children nor have custody of them should be required to pay full maintenance.

Reference

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Consumer Choice: The Key to Educational Quality?

Ken Gannicott, Taking Education Seriously: A Reform Program for Australian Schools, The Centre for Independent Studies, Sydney, 1997

Reviewed by Brian Crittenden

THIS book provides a clear assessment of what are called 'charter schools' in the United States, where they are rapidly spreading. Ken Gannicott, a Professor of Education at the University of Wollongong, strongly supports their introduction in Australia, ultimately to the extent of replacing the present government system. For the most part, he relies heavily on the language and images of economic analysis: education is a commodity; schools are the agencies through which it is dispensed; the crucial issue is how the providers and the customers are related in the transaction that is the central business of schools. As the book is about primary and secondary education, Gannicott almost always regards parents as the customers, with only an occasional reference to students in this capacity.

Gannicott notes that Australia now spends about twice as much, in real terms, on primary and secondary schooling as it did 20 years ago. Government schools are, on average, more costly than non-government schools (Catholic schools being, on average, the least expensive). The common justification for the increased spending is that it leads to better education. However, while there are no effective measures for many desired outcomes (and strong opposition from teacher unions to any comparative assessment), the available evidence from national and international tests indicates no general improvement in academic performance over the two decades. A substantial minority of students fall below minimally desirable levels. Recent studies of final year results suggest that, even with adjustment for differences in socio-economic background, government schools perform less well than Catholic and other private schools. Although OECD surveys have indicated no significant difference in student achievement for class sizes in the 15-40 range, much of the additional funding in the past two decades has been spent in government schools on employing more teachers in order to reduce class size.

While acknowledging the complexity of assessing educational production by using quantitative measures of input and output, Gannicott is satisfied that it is a reliable approach. He does note, however, that there is the further question of determining the underlying causes of the economic efficiency or otherwise that the quantitative measures show. In his view, the most important of these causes in the case of government schools is that they are producer dominated.

Qualitative analysis of individual schools has produced a predictable list of characteristics that make for an effective school. The 'effective school' approach has influenced policy for government schools in recent years. The main change has been a shift to greater self-management at the individual school level. However, after nearly a decade, there is no strong evidence of improved educational output. This is largely due, Gannicott claims, to the limited adoption of self-management.

The school-based administrative bureaucracy has increased in both government and non-government schools over the past six years. The total bureaucracy is now bigger than the central-regional one it has partly replaced; and, in any case, the devolution of decision-making to each school's principal and classroom teachers keeps the emphasis firmly on producer control.

Gannicott agrees that the establishment of selective and specialist government high schools and the end of zoning are desirable moves in the direction of some degree of consumer control. But the producer remains dominant, and unsuccessful applicants for a school usually outnumber those who gain enrolment. The most important reform we need, Gannicott claims, is a substantial increase in the supply of autonomous schools, in both the public and private sectors. The key to higher-quality educational outcomes is to break the dominance of the providers and enable consumers (parents) to apply more pressure of competition on those who offer educational 'goods'.

This is the special virtue Gannicott sees in 'charter schools' and for which they receive his enthusiastic support. They not only break down producer monopoly in the government system, but ensure that what is being offered as education is substantially subject to consumer choice. They are publicly owned and funded schools, but self-governing under the terms of a performance contract. They can be established by a group of parents, a local community, teachers, a university, and so on; and they may be run as profit or non-profit organisations. While they are free from many government and union restrictions, the proposal for such a school must set out how it will be conducted and, in particular, the details of its educational programme and the way its objectives will be assessed. These proposals (forming the 'charter') are to be approved by an appropriate public body. Approval of the charter would normally be for a period of three to six years. It would be revoked if the school failed to meet the tests of achievement set out in its charter. Details of each charter school would be widely published so that parents could make informed choices. Students who enrolled would bring the same per capita funding as for other public schools. 'Set-up' funds and capital costs would also be provided, as for other public schools. (I am not sure whether Gannicott includes profit-making charter schools in the public scheme.)

Charter schools could exist as a supplement to the public system. But Gannicott proposes that they should gradually replace it entirely. He is confident that public education provided wholly through these schools would ensure substantial autonomy at individual school level, and a range of options that would give customers the opportunity for meaningful choice. In these conditions of genuine competition, he does not doubt that the quality of the educational product of schooling is bound to be enhanced.

Although there are many points on which this book can be criticised, I shall restrict my comments to two pervasive features of its analysis and argument. First, the model of buying and selling a product in a competitive market is far too narrow for a good such as education. It grossly underestimates the complexity of what constitutes a worthwhile education; or, if the term is used normatively, what criteria dis-

tinguish education from indoctrinating and the many other forms of miseducation. Even when defensible criteria are established, it is a difficult task to assess the quality of actual processes and outcomes that claim to meet these criteria.

Although Gannicott acknowledges that the personal and social benefits of formal education are not just economic, it is the economic that he stresses: 'education is, after all, part of the information industry' (pp. 61-2). He often makes glowing comments on the quality of Asian schools as endorsed by their contribution to the 'rapidly growing economies' in that area. On this criterion, does the recent financial collapse in Asian countries cast doubt on the educational quality of their schools?

Despite the title of the book, it does not address in any thorough way the basic question of what primary and secondary schools should be doing in the name of education. The list of references is very thin on writings that treat this question.

Second, the proposal for charter schools is open to a number of objections. Gannicott is excessively optimistic about the capacity of parents to make sound judgments on the educational quality of schools. As is well known, choice is often based on a school's high tertiary entrance scores, even though such results leave open the question of its educational quality. A number of recent studies (relating to family health, nutrition, drugs, gambling and so on) would, at the least, indicate caution about a scheme so heavily reliant on informed and responsible choice being exercised by most parents in our society. In any case, giving the customers what they want in the name of education is not a sufficient condition for its quality.

Although Gannicott acknowledges that schools contribute to common economic and other benefits as well as to private interests, he neglects the crucial role of schools in relation to the cultural, political and other dimensions of a society's common good. These are not simply 'spillover' or 'external' benefits; they are integral to the process of education. Among the consequences are the degree of public supervision that should be exercised over schools, and the conditions that apply to what parents, students and others may choose in the name of education. Gannicott defends strong constraints on the former, and very little on the latter. His discussion does not even refer to John Dewey, the foremost theorist in defence of a common school system in a pluralist democracy. (I have attempted to discuss the complex issues, including a criticism of Dewey, in my *Parents, the State, and the Right to Educate*, Melbourne University Press, Melbourne, 1988.)

To be sure, there is a place for charter schools. However, I believe that an appropriate public body should exercise more detailed supervision than Gannicott seems to allow. This would include setting and monitoring standards of teacher competence, and general curriculum guidelines. Such a body would represent the justifiable interests of the whole society in the conduct of our schools. What schools do in the name of education is not simply a matter for parents of school-age children. Charter schools might develop to the point where they replaced the present public system. But they are only one alternative, not without limitations of their own. Certainly, they should not be promoted to the neglect of other ways in which the educational quality of our schools can be improved.

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Commonwealth Economic Policy and Education

Simon Marginson, Educating Australia: Government, Economy and Citizen since 1960, Cambridge University Press, Melbourne, 1997

Reviewed by Alan Barcan

THIS book is the product of a doctoral thesis on 'Markets in Education'. Its strengths include its wealth of statistics and its thorough scrutiny of documents, Australian and foreign, on economics and educational policy. But the scope is not as comprehensive as the title implies. It is a survey of Commonwealth government policies only. The neglect of policies in the States and Territories, the major providers of school education, obscures the varying patterns across Australia. Failure to consider the curriculum, examinations and assessment obscures the effectiveness of educational policy.

Though the son of two Old Left Melbourne University Labour Club personalities, to whom he dedicates his book, Marginson adopts neither the interlinking of economic, social, political and intellectual arenas (with an emphasis on the first) popular with the Old Left of the 1940s and 1950s nor the more simplistic yet pretentious interpretations of the New Left of the 1970s and 1980s, with its heavy theory, relativism, anti-humanism, and advocacy of white-collar and minority causes. This is a post-1987, post-Marxist radicalism. Yet one cannot call it post-modern, for Marginson has a consistent set of beliefs: he leans towards the critical theorists, the heirs of neo-Marxism. Fortunately, he avoids their educational jargon.

His views were shaped by a career as a research officer for the Australian Union of Students, the Victorian Secondary Teachers' Association and the Federated Australia University Staff Association. Since 1993 he has been Senior Lecturer at the Centre for the Study of Higher Education at The University of Melbourne. Marginson is one of a new breed of educational commentators. They have little or no expertise in teaching in schools or in writing history or sociology. Their strengths lie in economics or political science. Bowles and Gintis applied such skills for the New Left in *Schooling in Capitalist America* (1976), Chubb and Moe for the New Right in *Politics, Markets, and America's Schools* (1990). Marginson first analysed the political economy of education in his 1993 book, *Education and Public Policy in Australia*. This latest book, like the earlier one, is hostile to the New Right and economic rationalism. Since Labor is as enthusiastic as the Liberals in applying economic rationalism to education, the book presents an impression of objectivity.

The new analysts of educational policy bring a new interpretation and a new terminology. Social class is no longer a dominant concept. In his Preface, Marginson identifies some major themes: modernisation (a neutered substitute for 'reform'); the educational relevance of changing forms of citizenship; 'the growing sophistication of liberal government' (presumably this means the use of a bureaucratic intelligentsia in decision-making); a political economy of competition and markets (bringing a shift from public provision to market systems); and the impact

of this change on 'participation' and 'equity' (thus accommodating the special interest groups or 'disadvantaged minorities'). He makes the politically correct genuflection to 'insights derived from Foucault' but happily the French savant is thereafter almost invisible.

The introduction takes a sour look at current Coalition education programmes and briefly discusses the concept of citizenship. It could well have been omitted. Chapter 2 ('The Expansion of Education to 1975') examines the growth of Commonwealth financial commitment with the support of eleven statistical tables (the book has 51 such tables; only Chapter 9 has more than Chapter 2).

Chapter 3 ('The Karmel Report and Educational Quality') contains some good material. Marginson identifies the report as the most influential of all education reports in the postwar period. It 'connected to the radical egalitarian and progressivist values of the time' (p. 54). Chapters 4 ('The New Right and Public Policy' and 5 ('Individual and Government') are heavy with political economy. They present in a complicated way the challenge of monetarism to Keynesian theory, the rise of the New Right, the translation of these new economic theories into policies in the 1980s, fiscal policy after 1975, and the growth of market liberalism. Chapter 6 ('The New Right and Education') provides a critique of the New Right's view of education in the 1970s and 1980s. Marginson gives two paragraphs to the new education of the late 1960s and early 1970s which 'made the work of educational institutions more ambiguous and difficult, problematising the notion of singular academic and behavioural standards' (p. 129). He looks into the abyss and sees merely ambiguity and difficulty.

Chapter 7 ('Education and National Economic Reconstruction') brings us to the reconstruction of education which started about 1987-88 (Dawkins in Canberra, Metherell in Sydney). The rise of the service industries is identified through overseas analyses and confirmed by Australian statistics (Table 7.3, p. 170). The growth of the service industries is seen in economic and vocational terms, not in terms of changes in social class. After considering overseas documents on economic rationalism and education, Marginson effectively discusses the Dawkins revolution in higher education. But he makes no criticism of the destruction of the Colleges of Advanced Education in 1989. He treats changes in school systems in a very general way; his failure to consider events in at least some of the States deprives the book of the benefits of comparison. He discusses the new vocationalism (p. 167) without mention of the National Curriculum. 'Ministerialisation' is mentioned almost in passing but the explanation is myopic. Yes, it was 'associated with the imposition of economic agendas and the displacement of the role of the directors-general of education by generic managers ...' (p. 163). But Ministerial intervention was also provoked by the inability of the State Departments of Education to regain the controls they had lost in 1967-74 and by resentment of their close affiliation with teachers' unions. Marginson ably examines the growth of vocationalism, but does not mention that an important reason why the key competencies were embraced was to provide an alternative to external assessment, which teachers' unions opposed. They also provided employment for the educational bureaucracy.

Chapter 8 ('Participation and Equity') surveys the rising retention rate in schools from 1981 (in some cases from 1975) and the growth of higher education. Marginson records some important tendencies (for example, the vast growth in the number of postgraduate students) with very little comment. He provides a useful tabulated summary comparing the expansion of the 1960s to mid-1970s with that of the 1980s to early 1990s. He describes the shift from 'equality of opportunity' to 'participation and equity' and identifies a related shift in expectations among young people: 'official policies designed to transfer students' ambitions from the labour market to further education had achieved significant success' (p. 204).

In the title of Chapter 9, 'Economic Government in Education', the word 'economic' is used in the sense of 'cheap' or 'efficient'. Reductions in state expenditure was part of the crisis of the welfare state. The chapter roams across the years since 1975, disrupting the sense of historical progression and encouraging a sense of repetition. It would have been wiser to focus on 1987-93. Marginson examines Commonwealth expenditure on higher education, the abolition of free higher education and the spread of fee-based courses. After noting the widespread popular preference for private schooling, Marginson states that this encouraged the 1993 'Schools of the Future' programme of the Kennett Government in Victoria. He suggests the programme was 'partly modelled on the Thatcher reforms in Britain' (p. 240). In fact, Victoria owed a great deal to Metherell's example in New South Wales.

The final chapter, 'Civics, Citizenship and Difference', attempts to breathe life into the theme supposedly permeating the book. A social rationale is abruptly introduced. Disadvantaged minorities, republicanism, the national flag, land rights for Aborigines enter the discourse. Marginson attempts to trace the development of civics education in the schools; he does not mention the rejection of citizenship by neo-Marxist and neo-progressive educationists in the late 1960s. He presents a sketchy history of multiculturalism in the schools: 'Educators were required to renegotiate the balance between difference and unity' (p. 254). Some task! But it seems the schools have adopted official ideology. Marginson cites a study of Year 7 and Year 11 students in Western Australia who, presented with 26 possible attributes of a good citizen, ranked being well-informed about Australia's constitution and Australia's political system 24th and 25th. Highest support was given to respecting the rights of others and treating people equally regardless of gender, disabilities and race. Marginson comments: 'Given the growing recognition of diversity, it could be argued that the WA students had their priorities right' (p. 255).

Marginson identifies three unresolved issues in citizenship education: the role of history in the curriculum (which provides a chance to condemn John Howard's complaints about 'black armband' history); the possibility of a variety of specialised state secondary schools (Marginson sees no good reason why community groups should not sponsor specialised state schools); and the role of the media in education. 'Media, consumption and multi-media had now become the main source of civic identity and of understandings of difference'. They encourage a 'passive construction of a globalised self'. But formal education has the potential to provide

'technological literacy and critical skills enabling students to retain, enhance and construct their own chosen identities' (p. 258). The question (says Marginson) is whether these attributes will be monopolised by some students or would be available to all. But personal character, identity, is surely an ideological product based on a variety of social forces, such as family, social class, peer group, media, religion as well as formal schooling. Let us not overestimate what schools can do.

Marginson touches on the relationship of government and private schools at several places. He believes the 1973 Karmel Report 'enabled private schools to consolidate and strengthen, and pursue their social projects with growing success' (p. 60). As a result, government schools faced 'increasing pressure from a growing range of low cost alternatives' (p. 65). In fact, the shift of enrolments from state to non-state schools which started in 1977 continued despite rising fees. Funding may have kept fees a little lower than otherwise. A variety of factors encouraged the drift to private schools, including religious loyalties.

Marginson cites Karmel, who sent his own children to private schools: 'We won't sacrifice our kids to our principles' (p. 70). He mentions without comment that many parents had 'a desire for elite schooling' (p. 238). The eagerness of Labor politicians and state school teachers who could afford it to send their children to private schools suggests they were concerned about the quality of state schools.

According to Marginson, policies primarily intended for the renovation of Catholic schools 'were to be used by the Seventh-day Adventists and the Lutherans to set up school systems of their own' (p. 65). He chose bad examples. The Seventh-day Adventists already had a school system. They initially rejected state aid, yet their schools increased in number. In 1968 they reluctantly accepted funding for capital works, but only in 1983 for salaries. The Lutherans also had a school system. This benefited from state aid, but even more from ethnic funding, which first started in South Australia. In 1981 the Commonwealth set up its Ethnic Schools Program. Many of these ethnic schools were also religious schools.

The half-hearted incursion into the area of private schooling is matched by an equally hesitant approach to the curriculum. Marginson identifies three educational currents in the New Right in education. Employers wanted a more vocational curriculum; 'cultural conservatives' wanted more discipline, tougher selection and traditional values; and 'market liberals' wanted economic reforms — the application of private enterprise and free competition between educational institutions. Marginson does not discuss the curriculum changes which had so alarmed the 'cultural conservatives'; he merely provides a succession of New Right complaints torn out of context. He expects the reader to accept his assurance that these complaints are reactionary, anti-democratic, anti-egalitarian.

Preparing this book, says Marginson, was a labour of love but 'a labour that makes no financial sense' (p. xv). It is not, I imagine, for undergraduates; the content is too complex and demanding. But as a scholarly book it will be of use to some postgraduate researchers and academics.

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Chasing the Ecologically Sustainable Development Mirage

State of the Environment Advisory Council, Australia: State of the Environment 1996, CSIRO Press, Melbourne, 1996

Reviewed by Ian Wills

THE National Strategy for Ecologically Sustainable Development adopted by all Australian governments in 1992 calls for regular reports on the national state of the environment to enhance the quality, accessibility and relevance of data relating to ecologically sustainable development (ESD). *State of the Environment 1996* is the first such report, undertaken by the Commonwealth-appointed State of the Environment Advisory Council. Advisory Council members were directly responsible for the two introductory chapters and the final chapter, 'Towards Ecological Sustainability', which identifies key issues in, constraints on and information needs for better environmental management. Groups of experts prepared the seven intervening chapters on human settlements, biodiversity, the atmosphere, land resources, inland waters, estuaries and the sea, and natural and cultural heritage.

The report's conceptual structure is a modified version of the pressure-state-response model developed by the OECD. Each of the seven area chapters discusses, in turn, the human activities which exert pressures on the environment, the current condition of resources, and societal responses. Most results are reported in qualitative rather than quantitative terms. Summary tables at the end of each chapter list environmental components/problems and, for each component/problem, its present state, the adequacy of information, societal responses and an assessment of their effectiveness. In the concluding chapter, the Advisory Council identifies what it sees as the key issues arising from the report: the need for a systems-based approach to environmental management; loss of habitat and biodiversity; rural land degradation; high carbon dioxide emissions per unit of GDP; failure to integrate the management of land with that of adjacent inland and coastal waters; adverse environmental impacts of urban transport and waste disposal systems; and protection of the well-being and culture of indigenous Australians and of Australia's natural and cultural heritage.

State of the Environment 1996 presents a large amount of information in a relatively non-technical way. The writing is clear, if prosaic. Extensive use of colour-coded headings and subheadings makes the text easy to follow, and it is enlivened by liberal use of colour photographs. Numerous coloured charts, maps and tables illustrate and expand on arguments in the text. The authors use highlighted boxes to explain the complexities of scientific issues, definitions, administrative and legislative arrangements, and environmental policies and policy options. Although the report guides the reader to detailed sources, it does not itself provide sufficient detail for the specialists responsible for environmental management and policies. Yet its comprehensive coverage of environmental issues, readability and attractive

presentation should ensure that it is extensively read and quoted. It will no doubt be a staple source for secondary school projects in the years to come.

State of the Environment 1996 does a good job of describing the state of Australia's environment, but, in turning to diagnoses and policy prescriptions, it understates the scientific and behavioural uncertainty attending many environmental problems and policies. The Chair of the Advisory Council recognises the uncertainty problem in Chapter 1: 'In many important areas, Australia does not have the data, the analytical tools or the scientific understanding that would allow us to say whether current patterns of change to the natural environment are sustainable. We are effectively driving a car without an up-to-date map, so we cannot be sure where we are' (p. 1-7). One would therefore expect the Advisory Council and its chosen experts to concentrate on description and the science of environmental changes, and avoid unqualified conclusions about the appropriateness and effectiveness of Australian governments' environmental policies. But this is not the case. For example, the chapter on human settlements advocates expanded government roles in urban design and public transport planning to reduce car-based suburban sprawl. However, little attention is paid to the housing and transport preferences of urban residents, the problems of financing and managing public transport, and the susceptibility of governments to lobbying by urban pressure groups.

Another major problem with the report, related to inadequate scientific understanding, is the lack of integration of material across the key areas of the environment addressed in the seven area chapters. The expert groups are doubtless well qualified to assess problems and policy responses within their particular areas of expertise. However, their conclusions relate to particular facets of the total picture of human-environment interactions. The introductory and concluding chapters do not integrate the area chapter results, because the Advisory Council has no clear model of the totality of human-environment interactions in Australia. Thus, while the individual area chapters are valuable compilations of information in their own right, it is unclear whether the policy responses discussed in the chapters are consistent in physical, biological and behavioural terms. For example, it is possible that land use controls designed to protect biodiversity or natural and cultural heritage may, by reducing commercial returns from agricultural or pastoral operations, cause farmers to alter operations to the detriment of land resources or inland waters.

The State of the Environment Advisory Council advocates a systems-based approach to environmental management. But it never addresses the inconsistency between a systems-based approach and its own compartmentalisation of environmental issues according to key areas of the environment. Thus, Chapter 10, ostensibly an assessment of progress toward the overarching goal of ecological sustainability, in fact simply identifies what the Advisory Council sees as the key environmental management issues arising from the preceding area chapters.

The Council does recognise, in Chapter 10, the impediments to effective ecosystem management posed by compartmentalisation of problems according to the jurisdictional boundaries of governments and departments. It commends the Great Barrier Reef Marine Park Authority and the Murray-Darling Basin Commission as

'innovative structural solutions to complex management problems' (p. 10-27). However, consistent with its general avoidance of behavioural issues, it eschews suggestions regarding what might be done about political, economic and administrative barriers to changed environmental management.

The lack of analysis of human behaviour is a further major weakness of the report. While the authors focus on human activities as the causes of Australia's environmental problems, they pay little attention to the ways in which people's preferences and Australian society's administrative structures and rules governing natural resource use contribute to those problems. Australians' actions are criticised, but not analysed. Yet sustainable use of Australia's environment depends as much on understanding why people, in their roles as consumers, commuters, manufacturers, farmers, and so on, use natural resources in ways which harm others as it does on understanding the physical and biological consequences of those actions for the condition of the environment. How can the authors sensibly assess the effectiveness of governments' policy responses in the absence of information about people's preferences, information and options, and about political and economic constraints on policy choices and implementation?

The lack of behavioural analysis would be understandable if *State of the Environment 1996* were simply the first in a continuing statistical series reporting quantitative environmental indicators. However, as previously indicated, the pressure-state-response information in the report is mostly qualitative, and thus of limited value as a baseline for continuing environmental monitoring. Indeed, in Chapter 1 it is pointed out that the report is only a first step: 'Development of a nationally agreed set of environmental indicators is ... a complex task that will take a number of years to complete ... It will be necessary to progressively identify a scientifically credible set of environmental indicators and associated monitoring requirements' (p. 1-8).

The lack of behavioural analysis contributes to frequent incomplete or faulty economic reasoning. For example, the report judges efficiency of resource use in human settlements on the basis of resource use and waste production per head of population, without considering the quality of life, time and energy sacrifices in alternatives involving less resource inputs and more recycling. Again, it advocates uniform environmental standards across Australia, without considering the different benefits and costs of uniformity due to differences in the local environment, population and people's circumstances. The Advisory Council suggests that modern food production is less energy efficient than past 'household food self-sufficiency', without considering the energy-consumption consequences of spreading the population across the arable landscape. It applauds container deposit legislation in the face of doubts that it increases resource-use efficiency. But there are examples of appropriate balancing of benefits and costs: for example, the authors of the land resources chapter point out that pest animal eradication is generally unrealistic, because the costs of control per animal increase with decreasing pest densities.

The Advisory Council's pursuit of suitable environmental indicators has been seriously handicapped by tying it to an imprecise policy goal, namely, ESD. De-

defined as 'a pattern of development that improves the total quality of life, now and in the future, in a way that maintains the ecological processes on which life depends' (p. 10-4), ESD has been an agreed goal of all Australian governments since 1992. Yet, as described in Chapter 10, ESD is no more than agreed lists of broad objectives and guiding principles.

ESD cannot serve as the basis for state of the environment reporting. At present, we know too little of the functioning of natural ecosystems and human societies, and of the interactions between the two, to be able to agree on a precise definition of ESD, to measure it, and to move economic-environmental systems towards increased sustainability (Common, 1995:ch.3; Wills, 1992). Without detailed scientific and behavioural information about the trade-offs between the at-some-point-conflicting objectives listed in Chapter 10 (for example, biological diversity and maintaining Australia's international competitiveness), it is simply impossible to chart a path to a sustainable future. Yet, as a slogan denoting commitment to the environment, ESD has a firm hold on the minds of political decision-makers, who foot the bills for reports on the state of the environment. This may explain the discrepancy between the Advisory Council's stance in Chapter 1, where its Chair writes of 'driving without an up-to-date map', and Chapter 10, implausibly titled 'Towards Ecological Sustainability'.

The Council would do better to maintain its initial stance throughout. Admitting our inability to define and implement ESD, it could concentrate on using available scientific and behavioural information to select a provisional set of indicators of the state of the environment, based on the results in Chapters 3-9. As knowledge of the physical, biological and ecological functioning of the environment and of human interactions with the environment improves, the initial set of environmental indicators could be progressively revised, as advocated on page 1-8 of the report.

As it is, an opportunity to educate people about the complexities and uncertainties of human-environment interactions is largely squandered. Australians may be encouraged to believe that human-environment interactions are much better understood, and welfare-enhancing environmental policies much easier to identify and implement, than is in fact the case. So while the descriptive material in *State of the Environment 1996* will be valuable in increasing Australians' knowledge of particular environmental resources and problems, the overall effect of the report may be to encourage demands for ill-informed quick solutions to complex problems.

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NON-AGENDA

With the view of causing an increase to take place in the mass of national wealth, or with a view to increase of the means either of subsistence or enjoyment, without some special reason, the general rule is, that nothing ought to be done or attempted by government. The motto, or watchword of government, on these occasions, ought to be æ Be quiet. . . Whatever measures, therefore, cannot be justified as exceptions to that rule, may be considered as *non-agenda* on the part of government.

— Jeremy Bentham (c.1801)

New Zealand's Proposed 'Code of Social and Family Responsibility'

Andrew Mikkelsen

THE New Zealand government, as part of a policy designed to reduce the cost of welfare by making beneficiaries accountable for their benefits, has canvassed a proposed 'Code of Social and Family Responsibility'. The proposal sets out eleven 'expectations' for citizens, and especially beneficiaries, to be responsible in their lives. Because the Code is widely thought to represent a shift away from state welfare, it has been criticised by the political left, and praised by the political right. But on this issue, at least, the left is right, but for the wrong reasons. In fact, the proposed Code increases the influence of government, and does not go far enough towards reducing the government's role in welfare provision.

The Code's Eleven 'Expectations'

The proposal for a Code¹ sets out the following 'expectations' of New Zealanders:

1. Parents should love, care for, support and protect their children.
2. Pregnant women will protect their own and their baby's health with the support of their partner. They will begin regular visits to a doctor or midwife early in pregnancy.

¹ Web site <http://www.govt.nz/dsw>.

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3. Parents will do all they can to keep their children healthy. They will make use of free checks and immunisations, and seek early advice and treatment for sick or injured children.
4. Parents will do all they can to help their children learn from the time they're born.
5. Parents will take responsibility for seeing that their children are well prepared for school, and attend every day ready to learn.
6. Children must not break the law. Parents will take responsibility for bringing their children up to be law-abiding members of society. When children do offend, families, communities and government agencies will work together to prevent reoffending.
7. Parents will love and care for their children, support them financially and, where possible, share the parenting responsibilities, even when they are not living together.
8. People will take responsibility for developing the skills and knowledge they need to help them get a job, or take on a new job.
9. People receiving income support will seek full-time or part-time work (where appropriate), or take steps to improve their chances of getting a job.
10. People will manage their money to meet the basic needs of themselves and their family.
11. People will do all they can to keep themselves physically and mentally healthy.

The government invites the public to indicate whether they support such a Code and whether they think it should be used as a set of guidelines, incorporated in government policy, or passed into legislation.

Monitoring Expectations

It is not made clear how compliance with the expectations would be monitored. However, the transfer of information between government departments is a clear option. Under Expectation 3, the discussion document asks whether up-to-date immunisation should be a requirement for entry into early childhood education and schools. Immunisation status would most sensibly be monitored by the government cross-referencing information between the public health system and the public education system. Under Expectation 2, the question is asked whether the government should use the contact it already has with women receiving pregnancy-related sickness benefit to check whether they have sought proper pre-natal care.

A government anxious to control welfare spending would be likely to collect information only from institutions with which it had some formal connection, so that the great majority of people subject to the government's expectations would be

those using government welfare services. Thus, pregnant women receiving sickness benefit who use the public health system would be monitored by the government, but not those who are financially secure and who use the private health system.

This likely reliance on *public* information, which would lead to different groups who exhibit the same behaviour being treated differently, suggests that the Code is concerned with personal responsibility only insofar as it relates to the use of government-funded services. It reinforces the implication in the discussion document that the true issue is not responsibility as such, but the continuing cost of the social welfare system.

Public Reactions

Critics of the Code argue that it is a step towards treating welfare as another commodity to be privatised in the manner of telecommunications and electricity. They lament, on one hand, the government's apparent retreat from welfare, and, on the other, the government's proposal to require beneficiaries to perform certain acts as a condition of receiving benefits. Supporters of the Code, meanwhile, welcome it because it introduces some measure of accountability for welfare beneficiaries by requiring them to use their benefits responsibly. The general public appears, on balance, to support the proposal.

Yet very few commentators have focused on the long-term implications of the proposed Code. As in past debates about New Zealand's reforms, both critics and supporters of the proposal confine their argument to the implications of the Code for economic efficiency. But even if the proposed Code is economically efficient, it represents an unacceptable expansion of state intervention.

Arguments For the Code

One argument for the Code is that the government is entitled to require welfare beneficiaries to behave in certain ways as a condition of receiving benefits. Just as benefactors to private charities have a legitimate interest in the way their money is used, so taxpayers have a legitimate interest in the government's use of their money. In this way, the welfare of the tax-paying public is protected, as well as the welfare of recipients.

This argument overlooks a fundamental difference between private institutions and government. The difference is that the government, unlike private institutions, operates by legislating to finance and carry out its activities. While conditions on welfare may be wholly appropriate when imposed by a private person or institution, they are inappropriate when imposed by government. In the case of a private institution, the money transferred to the recipient is a gift, and may be given upon the express understanding that conditions will be observed. But in the case of government welfare, the money has been taken by force, and no clear intention can be inferred on the part of the benefactor for conditions to be imposed.

Another argument for the Code is that love and morality are economically efficient, as people will tend to spend money wisely on the things or people they love.

Similarly, responsible behaviour is likely to use resources more efficiently than irresponsible behaviour. But although morality and responsibility may well be economically efficient, and the Code may promote these, that provides no legitimate basis for the government to determine how private relationships which have no bearing on individual rights should be conducted.

In a market society, economic freedom and personal freedom are closely linked and are often secured through the same means. As a result they are often confused. However, the central danger of big government lies not in its impact on the economy, but in its impact on personal freedom by forcing citizens to live and behave in certain ways that have nothing to do with the protection of rights. However beneficial the Code could be in promoting economic efficiency, it still poses a threat to personal freedom. Apparently minor, pragmatic interventions may not, by themselves, amount to serious intrusions into personal liberty, but they have the potential to become so over time.

The principle of the rule of law holds that every citizen is equal under the law. But the Code does not treat people as equals. It seeks to make distinctions between people according to the values by which they live. Even if the Code is not embodied in legislation but is retained merely as a set of guidelines, those who choose to ignore it risk being treated unfavourably by government, regardless of whether they are violating anyone's rights. But the state's job is to enforce the law, not to encourage people to be 'responsible'.

The problem of the high and rising cost of the welfare state has arisen largely because welfare policies have created incentives to irresponsible behaviour. The Code is, in effect, an attempt to offset the undesirable consequences of the welfare state with further interventions. It is not likely to be successful. The only way to undo the harmful effects of welfare is directly to reform the welfare state itself, and to rely more on private welfare.

Conclusion

The current confusion about the proper role of government, even among market-friendly politicians such as New Zealand's Prime Minister, Jenny Shipley, illustrates the need for a strong principled basis for public policy.

New Zealand's reforms so far have occurred at the level of practical economics, without reference to freedom or the rule of law. The proposed Code is in the same mould, as the government is looking to it to help overcome the welfare expenditure problem. But straying from the rule of law in areas of social policy can have radical implications for individual privacy and freedom. And while the argument may be made that these measures are justified as increasing the economic freedom of taxpayers by giving effect to taxpayer preferences, the underlying assumption is still that the state must provide. If the government really wishes to address the problem of responsibility, it must set about removing the state from people's lives, in welfare as in other areas.