Chapter Five

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Mutual Recognition and Regulatory Competition[1]

Mutual recognition was legislated in Australia in 1992. It is proving to be a mere way station on the path towards the voluntary euthanasia of the States as regulators. The case for the continuation of mutual recognition is that, in the absence of regulatory competition, nationally-uniform regulations may be worse, even for big businesses, than are the inconveniences of mutual recognition.

1. Introduction and outline

Businesses that operate in more than one State prefer there to be no differences in the regulations that they encounter in the various States. However, nationally uniform regulation may mean more – rather than less – burdensome regulation of business.

The Business Council of Australia seems to regard mutual recognition as desirable, but generally inferior to complete uniformity or strict harmonisation.

An attraction of mutual recognition is that sometimes it may be obtained more quickly than either national uniformity or harmonisation. In Australia, fewer than three years elapsed between policy announcement and legislation. However, the process of working through difficult areas has not been so speedy.[2]

Mutual recognition within Australia of regulations relating to goods and occupations was legislated in 1992, and extended to include New Zealand in 1997. It was designed to reduce the costs incurred by multi-State businesses in satisfying more than one State's set of regulations; and to reduce barriers to inter-State movements of holders of occupational licenses. There were few exceptions, exclusions and exemptions.

For whatever reasons, mutual recognition is not a current focus of governments; quite the contrary. An *Intergovernmental Agreement for a National Licensing System for Specified Occupations* was signed by COAG (Council of Australian Governments) on 30 April 2009. The national licensing system will initially include relevant business and occupational licences in air-conditioning and refrigeration mechanics; building and building-related occupations; electrical; land transport (passenger vehicle drivers and dangerous goods only); maritime; plumbing and gasfitters. This Agreement implemented a *National Partnership Agreement* of February 2009, and followed the July 2008 meeting of COAG, where it was "...agreed that the seamless national economy initiatives were amongst the most significant and far-reaching of the potential reforms identified by COAG".

Under this "voluntary" *National Partnership Agreement*, which was urged by the Commonwealth, and carries the promise of Commonwealth-funded rewards, the parties committed to "...continuing to reduce the level of unnecessary regulation and inconsistent regulation across jurisdictions; delivering agreed COAG deregulation and competition priorities; and improving processes for regulation making and review". The States and the Territories "...will have responsibility to work together, and for many specific reforms to work jointly with the Commonwealth, to implement a coordinated national approach" in areas including occupational health and safety laws, licensing of tradespeople and health workforce.

The COAG agreements and processes of 2008-2009 are for centralised regulatory reform; and one move short of a Commonwealth takeover. Mutual recognition was the first step on a path leading

to that end point. Mutual recognition seems to involve a paradox: through mutual recognition, the States are simultaneously certifying that there are no essential differences in their regulations, while acting as though there are sufficient differences to justify their maintaining their own, different regulations. In granting "recognition" to the regulations or occupational registrations of another jurisdiction, a State is effectively certifying that the other jurisdiction's regulations or registration requirements meet acceptable standards.

If "your regulations are as good as mine", then why persist with different but similar regulations? Why not uniformity?

If uniformity were the dominant consideration, then mutual recognition is deficient. However, businesses complain not only of the lack of uniformity of regulations in the various States, but also of the burden of regulation generally, including Commonwealth regulation. Here, mutual recognition may have unappreciated advantages for business: inter-jurisdictional regulatory competition can in some circumstances reduce the overall burden of regulation, and without necessarily causing a damaging "race to the bottom".[3] Harmonisation and national uniformity eliminate regulatory competition within Australia, whereas mutual recognition does not. Where there is scope for regulatory competition, States that "get the regulations right" will gain at the expense of the others, through the attraction of more economic activity. This incentive vanishes if there is one regulator only.

This kind of argument is not easy to make in general, and is not readily illustrated with convincing factual evidence.

Section 2 of this paper sketches the arrangements governing mutual recognition within Australia and between Australia and New Zealand; and the rationales for mutual recognition of various kinds. The paradox of Australian mutual recognition is detailed in Section 3. Section 4 is about competitive federalism and mutual recognition. The case in favour of creating a seamless national economy is examined in Section 5 and, as usual in economics, I find costs as well as benefits. A passing glance is given to the High Court decision in *Betfair*.

2. Mutual recognition in Australia

> "The purpose of mutual recognition is to promote economic integration and increased trade between participants. It is one of a number of regulatory techniques available to governments to reduce regulatory impediments to the movement of goods and provision of services across jurisdictions".[4]

In 1990, Prime Minister Hawke noted that by 1992 the European Union would have created a trans-national economy more seamless than the Australian national economy.[5]

The context was the arguments and circumstances that led to the adoption of the National Competition Policy. After a series of Special Premiers' Conferences, in 1992 the Commonwealth, State and Territory governments signed the *Intergovernmental Agreement Relating to Mutual Recognition Agreement*, committing the parties to "establish a scheme for implementation of mutual recognition principles for goods and occupations for the purpose of promoting the goal of freedom of movement of goods and service providers in a national market in Australia".

The Agreement was given legislative form as the *Mutual Recognition (Commonwealth) Act* 1992, with the States either adopting the Commonwealth legislation or referring powers. A Trans-Tasman counterpart was passed in 1997. It was hoped that the schemes would operate with a minimum of bureaucracy.

Under the Act, goods that could lawfully be sold in one jurisdiction, having been produced there, or imported into it, could also lawfully be sold in a second jurisdiction, without meeting the second jurisdiction's requirements regarding production, presentation and inspection. This provision was

designed to remove what are called "indirect barriers" to the sale of goods. (However, a good that does not comply with the standards of a jurisdiction in which it is offered for sale must be labelled with State or country of origin information.)

For occupations, mutual recognition works through a process of "deemed" registration: registration in an occupation in one jurisdiction is sufficient grounds for registration in the *equivalent* occupation in another jurisdiction. However, anyone in a registered occupation wishing to work in a different jurisdiction needs to notify the relevant registration authority in that jurisdiction, except in occupations for which registration is nationally recognised.

Mutual recognition relates to occupations, not activities. Where a single license authorizes several activities in one jurisdiction, some of which have no equivalent in another, then equivalence can be achieved by limiting the scope of the mutually recognized licence, via the imposition of conditions.[6]

A safeguard is that any jurisdiction can refer to the relevant Ministerial Council a question about the standard applying in another jurisdiction to a good or to the practice of an occupation. Within twelve months the relevant Ministerial Council can determine, by two-thirds vote, what standard is appropriate to apply in all jurisdictions. The good or occupation in question remains subject to mutual recognition while the council deliberates. (Similar provisions relate to new goods, with the difference that a jurisdiction can temporarily exclude new goods from sale – e.g., on doubts about safety – that otherwise would be covered by mutual recognition.)

Also, a regulator can decline to register applicants from a particular jurisdiction. If an appeals tribunal upholds the decision to refuse registration, that itself can be taken to be a declaration that occupations are not equivalent, or that the difference in standards created risks for people or the environment. This would trigger referral of the question of standards to the relevant Ministerial Council.

There are some exceptions to mutual recognition (e.g., relating to health, safety, and the environment; and the manner in which an occupation is carried out); exclusions; and exemptions (e.g., firearms, pornography, endangered species, catch size).

It is useful to delineate various kinds of mutual recognition schemes, and identify the Australian one.

In his second reading speech, the Minister noted that:

> "The underlying premise for mutual recognition [within Australia] is that the existing regulatory arrangements of each State or Territory generally provide a satisfactory set of standards. Thus, on implementation of mutual recognition, no jurisdiction will be inundated with products that are inherently dangerous, unsafe or unhealthy, nor will there be an influx of inadequately qualified practitioners".[7]

Thus, Australia and New Zealand adopted a "comity" or "jurisdiction of origin" version of mutual recognition. Under this principle, each provider of a good or service can operate under the regulatory framework of its jurisdiction of origin. There was relatively little "pre-filtering" or harmonisation of core Australian regulatory provisions.

Any "duty of care" of an Australian State government should not extend to preventing a citizen from moving to another Australian State which offers what the first State regards as inadequate regulation. Under the principle of the "State of origin" or comity, should the "duty of care" extend to preventing a citizen from buying goods that are legal in the State of origin of the good; or services that would be legally supplied, if supplied in the State of origin of the supplier? If so, then mutual recognition of the Australian type does require States to be vigilant and effective in a most difficult set of tasks, which is to monitor the effects and enforcement not only of their own regulations, but also of the States (or countries) to which mutual recognition has been granted.

Comity distinguishes Australia from what happened, within the European Union, for services. Patrick Messerlin[8] has stated that mutual recognition within the European context requires the

effective harmonisation of the core provisions of regulations; and that this core is defined by negotiations between the countries or States involved. This implies a considerable dampening of inter-jurisdictional regulatory competition.[9]

However, after fourteen years under the legislation for mutual recognition, harmonisation has been initiated in Australia, partly in reaction to perceived "skill shortages". In 2006, COAG decided that Ministerial Councils should develop equivalence-tables for selected trades and, subsequently, for vocationally-trained registered occupations. This process proved transitory and, as noted above, is in the process of being displaced by a national licensing regime.

3. The paradox of Australian mutual recognition

The burden of this paper is that the case for continuing with mutual recognition, and not proceeding to harmonisation or uniformity, depends fundamentally on the case for inter-governmental competition within the federation. Without strong support from the argument in favour of preserving inter-governmental competition, then mutual recognition becomes a mere way-station on the path towards the euthanasia of the States as regulators in the spheres in which mutual recognition operates.

The primary purposes of mutual recognition are two-fold:

> 1. To eliminate, or at least reduce, the protection that State-based regulations afford "local" producers against competitors producing in or located in other States—this benefits customers and consumers directly (e.g., through greater choice or lower prices).
>
> 2. To eliminate, or at least reduce, any unnecessary or unjustified costs for the suppliers of goods and services, including labour services, of operating in more than one State, or of moving "residence" from one State to another – this benefits consumers and customers indirectly, as well as some suppliers of services, directly.

The motivation of mutual recognition is the creation of a seamless national economy, subject only to the frictions caused by justifiable differences in regulations in the various States. Yet the use of mutual recognition itself throws doubt on whether the resultant regulatory differences can continue to be justified.

The differences that matter, for the granting of mutual recognition, are those seen in the effects that are being sought through the regulations of one State compared with those of the other State; that is, differences in the degree to which the legitimate objectives of State regulation are met.

For a State responsibly to grant mutual recognition to a person registered to operate in another State as a social worker, say, implies a belief that there are no significant differences in the standards of customer protection afforded by the "importing" State compared with the "exporting" State (or that it is the responsibility of the client or customer to notice the differences). In other words, by granting mutual recognition the State is signalling that it is indifferent (or largely so) between its own regulation and the regulation imposed by the other State.[10]

However, if the differences between the regulations of the relevant States are implicitly acknowledged by the relevant States to be neither great nor significant, when judged in terms of the effects that are being sought through the regulations, then it seems that the differences in regulation are mere nuisances: that is to say, the adoption by all mutual-recognition States of the regulation of any one State, randomly chosen, would not make much difference to the outcomes, when judged in terms of the effects that are being sought, by each State, through their differing regulations.

So, mutual recognition seems to involve a paradox: mutual recognition permits differences in regulations across the States, but it should only do so if the different regulations make trivial differences in the attainment of the effects that properly motivate the regulations themselves.

In these circumstances, the obvious response of the Business Council of Australia or similar bodies, is to say the following: *Why not have uniform regulation? Choose one of the existing State regulations, any one, from amongst those of the States that have granted mutual recognition in the specific regulatory area. This would help create a truly seamless national market, and do so without any appreciable damage to the objects of regulation.*

A possible way out of this paradox – and maybe the only plausible route – is to appeal to the benefits of inter-governmental competition. The case to be argued is that, without inter-governmental competition in the setting of regulations, the regulations could be much "worse" than the existing set, and could result in larger unnecessary and unjustifiable costs to business or to the community at large, than occurs under mutual recognition.

4. Competitive federalism

For regulatory competition to be an advantage to business generally, it should reduce the burden of regulation on businesses. (Moreover, costly regulation may hamper small business more than big business.) What then are the likely effects of inter-jurisdictional competition via regulatory frameworks and practices? Does mutual recognition of the Australian kind merely (temporarily) preserve regulatory competition among Australian jurisdictions, or does it enhance it? (The negation of regulatory competition, national uniformity, is discussed in Section 5.)

These effects can be important: Messerlin[11] suggested that, under the "principle of jurisdiction of origin", the comparative advantage of a jurisdiction's service providers is determined by the jurisdiction's regulations, when combined with firm-specific technology.

In the absence of a cash reward from the Commonwealth, a State government may be motivated to alter its regulations to improve the welfare of its citizens generally – in the economic sphere, this requires an increase in economic efficiency. Its legislators and regulators may, for example, learn about better regulation from the experience of other jurisdictions, or from bodies like the Productivity Commission. Or governments may be more narrowly motivated, to increase the political support offered by specific types of households or businesses. These may either already be resident in the State or – and this is where my discussion will focus – induced to move into the State.

Businesses can "vote with their feet", by moving to a more attractive regulatory environment. In fact, the State imposing less costly regulation may still attract the factory, even if production costs are higher in that State. Professionals and trades-workers may be similarly attracted.[12]

Whether this change in location improves overall economic efficiency is an important question, not central to this paper. What matters here is whether mutual recognition enhances the rewards for successful regulatory competition, or not.

Within the ordinary commercial market-place, the comity version of mutual recognition means that a manufacturer located in, say, New South Wales can more readily than otherwise sell goods into Victoria, thereby providing more market competition within Victoria. Also, wholesalers and retailers can more readily source their supplies from inter-State, than previously. Similar remarks relate to occupations.

However, mutual recognition may also influence the choice of location of business and household. That is, mutual recognition not only facilitates greater goods-market competition and occupational mobility within Australia – which are the stated objectives – but also indirectly affects the degree of regulatory competition among the States.

Because the advent of mutual recognition did not require prior harmonisation of regulation in Australia, it did not remove or greatly reduce the scope for regulatory competition. Rather, my tentative conclusion is that for services, but maybe not for goods, mutual recognition in Australia may have enhanced the extent of inter-jurisdictional competition that is manifest through regulatory frameworks and practices.

Turning first to services: as there are no residency requirements for deemed registration for occupations, mutual recognition facilitates jurisdictional "shopping and hopping". Overseas professionals, say, psychologists, desiring registration in Australia, under mutual recognition may find it easier or faster initially to register in New Zealand than in any State; once registered, they can subsequently obtain Australian registration via mutual recognition. That is, it is reasonable to conclude that mutual recognition increases the incentives for a State to compete through offering a different regulatory environment.

Mutual recognition seems an attractive arrangement when a State wants to set a standard – say, by specifying the training required before licensing for an occupation – but recognises that there may be other acceptable ways of achieving approximately the same standard. Subject to the kinds of safeguards mentioned earlier, it seems that market choices should then be given free rein through mutual recognition, so long as consumers can know and evaluate the differences between the training given in one State and the other.

Mutual recognition may also stimulate the provision of more efficient training. For real estate agents, on-line training that is now available in Victoria for registration in Victoria provides competition to longer-established training providers in New South Wales. However, the New South Wales-specific aspects of New South Wales-based training may be sufficient to ensure its continued existence; and the training provided in New South Wales may better suit some budding real estate agents, including some planning to practice only in Victoria.

For goods, it is harder to make a plausible case that mutual recognition will enhance regulatory competition. Assume for example that, without mutual recognition, it would have been best for a firm to set up one factory in Victoria to serve the Victorian market, and another in New South Wales to serve that market. A single factory, having a larger scale of output, may have lower unit costs of production than those of two separate factories. But the operator of a single factory incurs the costs of two sets of regulations. For two separate factories to be the better choice for the firm (without mutual recognition), the benefits of scale of production should not be so large as to dominate the costs of regulation; and I will assume that is the case.

Under mutual recognition, this firm may instead choose to serve both the Victorian and New South Wales' markets from a single factory sited in one State or the other. The firm would locate where overall costs were lower, including costs of production and costs of meeting only one set of regulatory requirements. If the production cost conditions were similar in the two States, then the State offering the less costly set of regulations would more likely attract the single factory.

This is a somewhat contrived example, and may not be of great practical importance. I find it hard to devise more convincing cases.

Thus I reach the tentative conclusions that mutual recognition, which may bring advantages to consumers of the kind listed earlier (more variety, cheaper products), may also incidentally enhance inter-jurisdictional competition in the regulation of services; but maybe not of goods.

What then of a "race to the bottom"? In the taxation history of Australia, there is one famous example, the death of death duties. However, I cannot find a parallel Australian instance of a race to the regulatory bottom. Of course, spokespersons for various interests, offended or otherwise adversely affected by the application of mutual recognition, sometimes claim that the standards of another State (or Territory, or New Zealand) are so low as to threaten unjustified harm to their fellow citizens. However, the Productivity Commission, in its recent investigation of the Trans-Tasman scheme, did not come up with convincing instances.

Or a "race to the top"? The role of Ministerial Councils, in setting standards when there is a dispute, suggests that this is a distinct possibility under mutual recognition[13] (and maybe even more likely under national licensing systems – a possibility recognised in the Regulation Impact Statement for that system).[14]

And, as a general safeguard against a competitive race to the bottom (or top), our federal system provides the central government and Opposition, both ever eager to attract voters by selective

incursions into areas ordinarily left to the States, with an opportunity for redressing the balance between the costs and benefits of specific types of regulation, by promising to take it over.

5. Seamless national market

So far I have written this paper mostly as though it were advice to the Business Council of Australia and similar business lobby groups – be careful what you wish for. However, there are broader issues involved.

Two objectives – nation building, and national economic efficiency – have been advanced to support the case for the creation of "seamless national markets" and, in particular, for national uniformity of economic regulation.

When there are two goals, economists reflexively suggest that the single-minded pursuit of one goal can come at the expense of progress toward the other goal. Everything has its opportunity costs; the world abounds with trade-offs.

But in some instances, one goal may be pursued regardless of the cost to the other. A recent High Court case, *Betfair,*[15] is relevant. I took the Court to say that it should develop the law so as to deal with community and economic developments and (especially and maybe surprisingly) when they are embodied in government policy pronouncements, government actions, or governmental policy frameworks. An important passage was that:

> "[I]t must always be remembered that we are interpreting a Constitution in broad terms, intended to apply to the varying conditions which the development of our community must involve" (citing O'Connor J, at par. 19).

Relevant developments seemed to be three:

> 1. The *Ha* judgment (that the "exclusivity of federal power to impose duties of excise is not limited to the more modest purpose of protection of the integrity of the tariff policy of the Commonwealth").
>
> 2. The "new economy" – the significance of which I take to be that (actual or potential) customers and suppliers are no longer necessarily located in the same, fixed geographic area, like a State.
>
> 3. National Competition Policy (the significance of which I take to be that the policy of all Australian governments is that competition should be restricted only if the benefits of restriction exceed the costs that restrictions impose, when both are judged from the point of view of the whole community and not merely of sections of the community).

With those things in mind I read the judgment[16] to say the Australian Constitution should be interpreted as creating a nation; and this requires that there be an integrated national economy, and not a collection of fragmented State, regional, or local economies. The "political economy" aspect or purpose of Chapter IV, and especially of ss 90 and 92 of the Constitution, when read together, mean or imply that the Constitution was designed, amongst other things, to create national markets in order to assist with the creation of the Australian nation. Consequently, jurisdictional differences in regulations should be permitted only in very limited and shrinking circumstances.

A possible implication is that the creation of a nationally-integrated economy should be pursued regardless of the effects on national economic efficiency.[17]

In effect, the judgment ignored the kind of argument put by Messerlin, namely, that competition occurs not only between suppliers of marketed goods and services, but also between locations. That is, it was assumed that regulatory diversity in a federation was solely an impediment to competition, rather than being a form of competition itself.

The argument is sometimes made that the gains from national regulations grow larger, when the market spontaneously becomes more national. For example, the Productivity Commission[18] and the High Court in *Betfair* seem to accept this argument. But Henry Ergas[19] has made the counter-claim: when communications and transport costs fall, and businesses and consumers are more "foot-loose", less tied to local suppliers and demanders, then the payoff is increased to a jurisdiction from getting regulations "right". That is, when the costs of communications and travel are reduced, businesses will respond more to differences in the costs of regulation, so that the incentives for inter-jurisdictional competition are increased, not decreased.

What then is the relationship between the creation of a seamless national market, and national economic efficiency? Alternatively, what are the costs and benefits of inter-jurisdictional regulatory competition? Here, the empirical economic literature is not very helpful.

The Productivity Commission[20] was unable to make any quantitative estimate of the benefits of mutual recognition. And due to the nature of business records, it could not come up with an estimate of the costs imposed on businesses by inter-State differences in regulations. The Business Council of Australia[21] reported estimates of costs imposed on specific business firms by differences in selected State regulations, but attempted no overall estimate of costs.

In the paper cited earlier, Patrick Messerlin claimed that those EU countries that went their own ways and liberalised their regulations, were rewarded with higher growth rates of GDP. What he did not examine was whether these superior results were at the greater expense of growth in other EU countries. That is, Messerlin did not ask whether the delay in the progress towards a seamless EU market was costly to the EU as a whole (that is, "beggar-thy-neighbour"). Moreover, I am sceptical that econometrics can reliably estimate the net benefits of differences in policy and institutions across time and space. And ultimately, the purposes of economic, political and social life are as various as the people, and not readily captured in aggregates like GDP.

Using non-econometric techniques, which allow for values other than those that manifest as GDP, the Productivity Commission[22] has estimated net benefits could flow to the Australian community from the implementation of its suggestions for improved regulation of consumer matters, of between $1.5 billion and $4.5 billion a year. Although some of these large gains would be produced by correcting what the Commission identified as the inconsistencies, gaps and overlaps arising from the shared responsibility between governments, the major source of gain (as I read the report) was from the hypothetical implementation of a generally superior set of policies. That is, the Commission's estimates do not distinguish what benefits would flow from there being a more integrated national market, from those that would flow if all governments adopted roughly similar but better policies.

(For my taste, the Productivity Commission did not pay sufficient attention to the ideas that there is no one best way to aggregate individual preferences over matters like the trade-off between riskiness of consumer products and their prices; or that there may be no one best regulation.)

The COAG decision on national licensing was not backed by any quantitative estimate:

> "While it is difficult at this stage of the development of the national licensing system to quantify costs, overall the costs of putting in place a national scheme, regardless of the model used, are expected to be outweighed by its aggregate benefits to business, governments and consumers. The new scheme is anticipated to increase the mobility of licensed labour, reduce red tape and enhance efficiency. This will arise from the use of best practice principles of licensing coupled with more uniform standards and increased transparency of information available to regulators, business and consumers on the status and training of licensees".[23]

6. Conclusions

Henry Ergas[24] has provided a useful guide for locating various cooperative ways to reduce differences in regulations (below). On the right are referrals of power to a central government or to a "lead" State, to harmonise or nationalise the regulations; on the left are mutual recognition and other voluntary agreements between governments to reduce the extent of regulatory differences.

He has also provided a summary of the advantages and disadvantages of the various routes. (The advantages are in the middle row, and the disadvantages, the bottom row). For mutual recognition, the first disadvantage is the continuation of some costly differences in regulations, across jurisdictions. The second disadvantage that Ergas lists – a "race to the bottom" – is a possible, albeit unlikely concomitant of the main advantage of mutual recognition, which is that mutual recognition retains an element of intergovernmental competition. Of course, voluntary arrangements of the kind shown in Ergas' picture and table are not the only way to achieve uniformity of regulation. There seem to be few constitutional constraints preventing the Commonwealth from excluding the States from most regulatory fields.

In his insightful chapter on "The Federal Constitution", Alexis de Tocqueville, describing and analysing the US system in the 1830s, asserts that:

> "The federal system was created with the intention of combining the different advantages which result from the magnitude and the littleness of nations…".

He goes on to elaborate on the advantages of "littleness" by pointing out that:

> "In great centralized nations the legislator is obliged to give a character of uniformity to the laws, which does not always suit the diversity of customs and of districts; as he takes no cognizance of special cases, he can only proceed upon general principles … since legislation cannot adapt itself to the exigencies and the customs of the population, which is a great cause of trouble and misery".[25]

De Tocqueville, however, also wrote that:

> "I am of the opinion that, in the democratic ages which are opening upon us … centralization will be the natural government".

In Australia, the Labor Party has always been anti-federalist. Recently, this attitude seems to have become bi-partisan at the federal level. In the fiscal arena, centralization of revenue collection has increased – especially with the imposition of the GST, which is a Commonwealth tax. Greater efforts have also been made to supervise and control the pattern of State spending from Canberra: the independence and responsibility of the States, as spenders, has been reduced. As to revenues, the traditional theory of taxation supports the centralization or cartelization of taxes imposed on mobile tax bases and, as the costs of transport and communications fall, tax bases are becoming more mobile and so the traditional case strengthens. The only strong counter-argument – based to some extent on public choice theory – is that the decades of living on handouts from the Commonwealth have degraded the quality of State politics and policies. And that counter-argument becomes irrelevant, if the States did not exist.

Mutual recognition is a cooperative, partial solution to the inconveniences caused by the States in their roles as independent regulators of goods and occupations, and was designed to beneficially enhance competition in private markets for goods and services. It is based on the idea that the States

and Territories all meet their regulatory responsibilities to more or less the same degree. So mutual recognition carries a self-destruct button: if the various State regulations and regulatory regimes are effectively the same, and if differences cause costs, then why not abolish the differences?

The only possible but not decisive reply is that, when there is but one source of regulation, there can be no guarantee that the ensuing regulation will be less costly than what occurs under mutual recognition. There will no inter-jurisdictional differences, to be sure; but the one-and-only regulation may be worse, for business and others, than the competitive diversity that arises under federalism.

Endnotes:

1. This paper draws on an unpublished paper delivered at an IPAA conference in 2008, and has benefited greatly from comments from Henry Ergas, Patrick Messerlin and Kerry Corke.

2. See Productivity Commission 2009, *Review of Mutual Recognition Schemes*, Research Report, Canberra.

3. A comparison of the economic merits of mutual recognition and harmonization is beyond the scope of this paper.

4. http://www.coag.gov.au/mutualrecognition/index.cfm.

5. For background, I have drawn on the *Review of Mutual Recognition Schemes, op. cit.*.

6. *Review of Mutual Recognition Schemes*, *op. cit.*, p. xxxiv.

7. Free, R (Minister for Science and Technology), Second Reading Speech, *Mutual Recognition Bill* 1992, House of Representatives *Hansard*, 3 November, 1992, p. 2432; cited in Productivity Commission 2008, *Review of Australia's Consumer Policy Framework*, Final Report, Canberra, p. 32.

8. Messerlin, P, *Economic and Regulatory Reforms in Europe – Past Experiences and Future Challenges*, Richard Snape Lecture, 30 October, 2007, Productivity Commission, Melbourne, p. 26.

9. There is a third style of mutual recognition, more liberal than comity. It permits suppliers of goods or services a free choice of which jurisdiction's regulations to comply with. The Productivity Commission made a parallel proposal when it suggested that certain corporations should be permitted to choose to opt into coverage by ComCare, and opt out of State-based schemes for workers' compensation. See *National Workers' Compensation and Occupational Health and Safety Frameworks*, Productivity Commission 2004, Report No. 27, Canberra.

10. The protection of the rents of bureaucrats and others in the home State, while no doubt a strong motivation for the retention of a State's own regulation, does not qualify for the purposes of the argument, which is concerned with the long-term interests of the whole community, not mere sections of it.

11. Messerlin, P, *op. cit.*.

12. If one State's changes have dramatic effects, then it is more likely that inter-jurisdictional competition will lead others to copy. However, regulatory competition does not necessarily

suppress diversity in regulation.

13. Huddart, Hughes and Brunnermeier, in a model of competitive stock market regulations, conclude that "trading concentrates on high disclosure exchanges[,] prompting exchanges to engage in a 'race for the top' in setting their disclosure requirements to maximize trading volume". See Huddart, S, Hughes, JS and Brunnermeier, M, *Disclosure Requirements and Stock Exchange Listing Choice in an International Context*, Journal of Accounting Economics, 1999, pp. 26, 237-269.

14. One of the objectives of the national licensing system is to "ensure that licensing arrangements are effective and proportional to that required for consumer protection and worker and public health and safety, while ensuring economic efficiency and equity of access".

15. *Betfair Pty Limited v. Western Australia* [2008] HCA 11, 27 March 2008; at http://www.austlii.edu.au/au/cases/ cth/HCA/2008 /11.html.

16. Especially paragraphs [10-19], and parts of [21-49] and [85-105].

17. The argument has been made that the Constitution of the European Community, with its over-riding of local and national preferences (and therefore, allegiances), can be interpreted as a bulwark against war: see Brennan, G and Hamlin, A (2002), *Experience Constitutionalism*, Constitutional Political Economy, Vol. 14, No. 4, pp. 299-311.

18. *Review of Australia's Consumer Policy Framework*, *op. cit.*, Vol. 1, p. 18.

19. Ergas, H, *Harmonisation in a Federal System*, Presentation to the Australia and New Zealand School of Government Conference on *Making Federalism Work*, Melbourne, September 2008.

20. *Review of Mutual Recognition Schemes*, *op. cit.*.

21. Business Council of Australia, *Towards a seamless economy: Modernising the regulation of Australian business*, accessed via http://www.bca.com.au/content/99520.aspx.

22. *Review of Australia's Consumer Policy Framework*, *op. cit.*.

23. *National Licensing System for Specified Occupations*, *op. cit.*, p. 15.

24. Ergas, H, *Improving the delivery of public services in the federation*, Menzies Research Conference: *The Future of Federalism*, at http://www.mrcltd.org.au/research/Ergas-final.pdf.

25. de Tocqueville, Alexis, *Democracy in America*, 1855, translated by Henry Reeve (Barnes & Co., New York), Vol. 1, p. 173.