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Productivity Commission  
Disability Discrimination Act Inquiry  
LB2 Collins St. East  
MELBOURNE VIC 8003

Dear Sir/Madam,

I am an economist at the University of New South Wales, currently working on a book on the Economics of Disability. I would appreciate the opportunity to appear before the Commission when it convenes in Sydney.

I would also appreciate an extension of time to submit a paper to the Productivity Commission. I was going to submit an unedited draft, but have decided that it would be inefficient and unworkable to be sending continuous updates and revisions as the work evolves. As the end of the semester approaches and my teaching commitments slow down, I will be able to work more intensively on my submission and would welcome the opportunity to do so.

I would therefore appreciate it if you gave let me know a latest date for the submission. I would appreciate an extension till the end of June. I expect that the submission will be about 50 pages long. A summary of my submission is attached below.

If you have any questions, please feel free to contact me by any of the means outlined above.

Yours sincerely,

Dr. Jack Frisch

THE ECONOMICS OF THE DISABILITY DISCRIMINATION ACT

The thrust of my submission is that the DDA in principle enhances both economic efficiency and social justice, but fails in practice because of the ambiguity and uncertainty of the *unjustifiable hardship* clause and its reliance on a biased complaint-based enforcement mechanism.

Justification for the DDA: Equity and Efficiency of the Private and Public Markets

1. The enhancement of social justice can be argued along the lines articulated by Rawls, Sen, and Nussbaum. Rawls argues that society's welfare increases only if the welfare of the materially worst off is increased. His argument is ambiguous on whether people with disabilities are part of the social contract, but Nussbaum takes this up along the lines of Sen's "capabilities" approach. Sen has written extensively on the contradictions of GNP-accounting and utilitarian social welfare functions and has argued that social well-being is maximised when the state accounts for the varying abilities to convert endowments into production, and when the varying capabilities are equalised. Sen shows that social well-being is not maximised by accepting the income distribution that is implied by endowments but by equalising the capabilities with which endowments are converted into production.

*The Sen Capabilities approach to social utility is relevant insofar as the DDA is a means of enhancing the capabilities of people with disabilities who are otherwise disadvantaged by their natural endowment.*

2. Traditional microeconomic suggests that the market is inefficient in providing the goods and services pertinent to disability i.e. people are willing to pay more than the cost of an additional unit of production, yet for one or another reason, the market does not supply the additional product. The reasons for inefficiency lie in information asymmetry, non-contestability of markets, and externalities.

- a. **Information asymmetry** leads to there being no market for insuring against the additional costs due to long-term and permanent disability. As a result, people with disability and their families bear most of the additional costs of living that result from disability. The government partly fills the vacuum, but the same moral hazard issues that would plague private insurance markets also plague government mechanisms.

*The missing insurance market suggests that the value of a non-market institutional response such as the DDA might be measurable as the implicit premium that people would be willing to pay if the missing market was in place.*

- b. The small number of people with particular impairments and the heterogeneity of impairments imply that goods and services that are disability-specific are often **natural monopolies**. As a result, the price of these goods and services is often substantially above marginal cost. Given that many of these goods are necessities, and that the market demand is likely to be inelastic, the inefficiency is also likely to be high and the cost of living effect substantial.

*The natural monopoly which exists has no direct implication for the DDA other than to imply that the incomes of people with disabilities is biased down by the non-competitive market, and that this is likely to distort observed demand.*

- c. There are three sources of **externality** caused by ignoring the needs of people with disability in the design of goods and services.
- i. Many people with disability spend a great deal *time* overcoming and managing obstacles e.g. finding alternatives, phoning in advance, waiting for others, etc. because of the inadequacy of design. In the extreme, inadequate design and inflexible rules leads to *unemployment*.

The time spent unemployed and overcoming obstacles would better be used in productive employment.

- ii. The *associates of people with disability* also spend a great deal of time assisting people with disabilities overcome and manage the obstacles due to inadequate design.

In the extreme, inadequate design leads to underemployment or the inefficient employment of family members who would be more productive in alternative employment - to that of “caregiver.”

- iii. *Network externalities* occur where design issues are interdependent across products so that inadequacy of design in one good or services makes it uneconomic to provide adequate design in another service. Thus, an accessible bus system has little value if buildings are inaccessible and accessible buildings are of little value if the transport system is inaccessible.

Network externalities are extensive because participation in the community involves use of a wide range of goods and services as preconditions. Most people take these for granted but for persons with impairment, personal care, transport, building access and flexible scheduling etc... are inter-related.

*Without the DDA, there is no obligation for goods and service providers to account for the costs imposed on people with disability by inadequate design and (rules). As a result, there is less than optimal design for disability. The DDA obliges goods and service providers to design their products (and rules) to account for the costs imposed on people with disability.*

3. Market failure does not imply that government can efficiently fill the vacuum, and indeed, there are several sources of government failure in the provision of goods and services for people with disabilities. The most significant failure is due to the tendency for politicians to supply goods and services to the *median voter* rather than to the marginal voter.
4. Nor do the inefficiencies consequent to market failures necessarily imply that any alternative offers a more efficient solutions. The transaction costs of designing efficient and equitable policy involve real resource costs in administration, communication, co-ordination and distribution. Ideologues on one side of the disability policy debate imply that the transaction costs of “ideal” policy are overwhelmingly high and that such policy therefore cannot be implemented, while others imply that they are negligible and feel cheated in the lack of progress. In truth, the transaction costs vary from case to case and little is known about them. At this stage the DDA seems to offer a relatively low transaction cost instrument for progressing efficiency and equity towards people with disability.

Monopoly, externalities and asymmetric information undermine the “first-best” market solution to the issues posed by impairment. The heterogeneity of impairment, the importance of privacy, and the nature of the geographically based two-party political system undermine the “first-best” government solution to the problems posed by impairment.

*The DDA is undoubtedly the most important “second-best” public strategy to enhance the design of goods and services and to overcome some of the inefficiencies of the private and political markets.*

Problems with the DDA

1. The **uncertainty of the “unjustifiable hardship”** clause and the lack of proper enforcement undermine the DDA. People are rationally reluctant to make complaints where expected benefits are less than expected costs, with further reluctance where there is a high degree of uncertainty about the outcome. The reluctance increases where conciliation is likely to fail, and where court costs and uncertainties increase the expected costs of a complaint.
2. The principal mechanism for **enforcing the DDA** is through the complaints made by people who feel that they have faced discrimination.

Except for discrimination involving income loss (i.e. except for employment discrimination and education discrimination), the benefit from rectifying a specific single act of discrimination is likely to be small relative to the cost to the goods/service provider of overcoming the discrimination.

As a result, few people are likely to make complaints – even though many individuals might face the same single act of discrimination, and even though the same individual may face many small similar acts of discrimination continually on a daily basis. That is, there may be substantial discrimination but few complaints. The possibility of class action through the DDA has not been realised because of the high transaction costs of coordinating class action complaints relative to the perceived benefits, particularly in view of the uncertainty of the unjustifiable hardship clause.

3. Because of the inadequate definition of “unjustifiable hardship” in legislation, and because HREOC has not clarified the definition, complainants and respondents face a **high degree of uncertainty** in trying to ascertain the outcome and therefore the likely value of a complaint. This uncertainty increases the effective cost of making a complaint and thereby compounds the reluctance to make complaints.
4. **Ambiguity** of the concept of “unjustifiable hardship” exists on several matters of definition.
  - a. It is not clear to what extent the court may distinguish between the *actual incidence of cost and the real incidence*. The real incidence can differ from the nominal incidence because costs can be shifted backward to suppliers and forward to consumers, depending on demand and supply elasticity, and on the competitive conditions in a respondent’s industry.
  - b. The *denominator* in defining “unjustifiable” is unclear yet it makes a difference whether the cost of rectifying discrimination is related to profits or the size of assets. Furthermore, whether profits are defined as economic profits, accounting profits or tax profits is important since

they lead to different conclusions. Similarly, whether cost is relative to gross assets, net assets, or liquid assets, and whether potential borrowings are accounted for is critical to a determination. The accounting period for a determination and the corporate/legal structure may also be critical.

- c. The *threshold* for “unjustifiable” is also critical i.e. whether the cost to denominator ratio needs to be above 1%, 3% or 10% before it is unjustifiable will lead to different results.
5. The ambiguous legal status of HREOC determinations has undermined the HREOC conciliation process. The **economics of court resolutions** favours respondents (with greater access to capital, with tax deductibility of court costs, and with the possibility of follow-on cost implications) over complainants. Because of these biases, respondents can reasonably predict that complainants will not follow through to the Federal or Magistrates Court. As a result, respondents have little incentive to negotiate in good faith before HREOC. The possibility that complainants may be required to pay the costs of respondents if the complaint is unsuccessful compounds the bias.
6. The unjustifiable hardship clause has effectively **limited the scope of the DDA** to non-competitive industries and non-profit organisations, including government and semi-government organisations.

Firms in competitive industries generally cannot pass the incidence of a differential cost impost either forward or backward and therefore bear 100% of any impost that is not born by other firms in the industry. Because firms in competitive industries generally earn no economic profit, firms in competitive industries can arguably always claim a burden, and given the ambiguity of the unjustifiable hardship clause, are likely to claim it.

With increased information and communication technology, and increased mobility of capital and labour markets, competition has increased over the last 20 years, and to that extent, the scope of the DDA has thereby diminished over that period.

7. The unjustifiable hardship clause has also effectively biased the scope of the DDA to **prospective acts rather than retrospective practices**. This is because it is far more expensive to rectify discrimination based on past practices than to prevent future discrimination, and therefore more likely that existing discriminatory practices will be justifiable while future designs will not.

This sort of bias is economically efficient, but it implies that the **impact of the DDA is likely to show up only slowly**. In view of the extensive network externalities involved in remedying disability, participation in the community will lag implementation outcomes in the various components. Thus, even if

the building infrastructure is fully accessible, participation will not increase significantly until the transport infrastructure, the social security system, the personal care services etc... are seamlessly integrated into the totality of disability participation.

8. Despite the uncertainties, the DDA was initially effective in enhancing the opportunities of people with disabilities. Arguably this has been because many large firms and government organisations instituted and implemented **Action Plans** which could be used as another defense against a complaint. The Action Plans have been useful as a means of focusing organisational consciousness about how to remedy discrimination and they have arguably led organisations to implement strategies that they would not have implemented without the DDA. It is unlikely that organisations will monitor, review, implement and update their Action Plans if they come to view the DDA as legislation without enforcement.

## Conclusions

1. An effective DDA is justifiable on economic efficiency and equity grounds.
2. The unjustifiable hardship clause is ambiguous and inefficient and therefore needs clarification. The ambiguity means that some complainants make claims they would not otherwise make, and some complainants do not make claims that would be justified. The uncertainty has led to the DDA becoming ineffective, particularly following the ruling that HREOC determinations are unconstitutional.
3. Complaints are an ineffective form of enforcement. People with disability who face acts of discrimination will not make a complaint if the expected benefits of an outcome are likely to be less than the expected costs. Respondents are likely to claim unjustifiable hardship if the cost of remedy is likely to be high and greater than the costs of defense. The net effect is that there are unlikely to be complaints – even when the aggregate social benefits of corrective action are greater than the aggregate costs.
4. The network externalities together with the biases and uncertainties of an enforcement mechanism based on complaints have together meant that progress towards including people with disabilities into the life of the community has been substantially slow. One implication is that participation data are unlikely to show a significant increase in participation even though there has been mild progress. For example:
  - Wheelchair users are not going to catch trains if they can't be guaranteed continuous path of travel throughout the network.
  - People with intellectual disabilities are unlikely to maintain steady employment if their colleagues continue to be insensitive.
  - Children with learning difficulties are unlikely to finish schooling if teachers continue to be unsupportive.

These issues are not resolved quickly. It takes time and perseverance.