

**Response to Commonwealth Grants
Commission Position Paper CGC 2009/03**

Treatment of Commonwealth Payments

November 2009



Treatment of Payments

Victoria generally supports the CGC treatment of payments proposed in position paper 2009/03. As outlined in previous submissions, Victoria considers that the guidelines adopted by the CGC are consistent with the Intergovernmental Agreement on Federal Financial Relations (IGA), which states that the GST is distributed to achieve horizontal fiscal equalisation. To achieve this aim, Commonwealth payments that have an influence on underlying State fiscal capacities should impact on GST relativities.

In paragraph 28 of its position paper, the CGC clarified its guidelines (see below) in dealing with the direct impact of Commonwealth payments to the States. Indirect impacts, including those relating to payments made direct to PTEs, are covered by the general assessment guidelines of the Commission¹.

- (i) Apply any treatment prescribed by the ToR, including to any on-going payments quarantined in previous ToR.
- (ii) National SPPs will have an impact on the relativities – these are available for State budget support and needs are assessed. The exception is non-government schools payments where their disposition does not impact on State fiscal capacities.
- (iii) All other payments should have a direct impact on the relativities unless:
 - they are a purchase by the Commonwealth;
 - they are for programmes implemented at the behest of the Commonwealth and which lead to above average or unique State outcomes (such as a trial programme which is not part of services delivered under average State policy);
 - they are a payment to a third party that has no impact on State fiscal capacities (States act as an intermediary and the payment does not reduce or increase State needs);
 - needs have not been able to be assessed for the State expenditures to which the payment relates².

Victoria supports the principle that payments that are available for normal State budgetary support and needs are able to be assessed should impact on relativities. These include all payments to government schools such as the government schools component of the Early Childhood Education and Literacy and Numeracy payments.

¹ NPPs and COPEs that have been treated so that they do not have a direct impact on the relativities can still affect State fiscal capacities. In those cases it may be appropriate to assess a disability factor to reflect this indirect impact.

² If an EPC assessment has been made because the Commission considers there are no differential disabilities or the assessment would be immaterial, then needs have been assessed.

Similarly, payments such as the Great Artesian Basin payment should impact on relativities because a deliberative assessment of needs has been made. These payments will directly support the delivery of core state services that affect State fiscal positions and hence should impact on GST relativities. Conversely, payments such as the Essential Vaccines payment should not impact on relativities because they are a Commonwealth purchase.

In examining each payment, Victoria considers that the CGC should consider the intent and form of each payment in deciding the appropriate treatment rather than decide a treatment for each class of payment. Consistent with the IGA, the CGC should have discretion to consider individual payments on a case by case basis.

General Revenue Assistance and Specific Purpose Payments

Victoria agrees with the proposed treatment of these payments by inclusion, recognising that these payments are available to provide general budget support to a State or Territory, with the exception of payments to non-government schools as these are payments to a third party.

National Partnership Payments

Victoria generally agrees with the treatment of these payments. However, there are some points of clarification which Victoria would like to raise with the Commission.

- We ask the Commission to clarify how it proposes to treat the Closing the Gap payments. These payments should be treated by inclusion, unless specifically excluded under the Terms of Reference, as they support the delivery of state provided services.
- The Remote Indigenous Housing (RIH) payments replace Australian remote Indigenous housing (ARIA) and Community Housing and Infrastructure Programme (CHIP) payments. All CHIP payments (including those paid to NGOs, the treatment of which was specifically changed in the 2009 Update) were treated by inclusion in the 2009 Update because the previous approach did not allow for interstate differences in the extent to which services provided by non-government organisations reduced the need for states to provide comparable services, and did not achieve equalisation. These payments impact on State finances and should therefore continue to impact on relativities. It may not be possible to discern the CHIP/ARIA split under the new framework. However, the RIH payments are around \$350 million, making CHIP almost 50%. The CGC should consider treating 50% of RIH payments such that they impact the relativities, to maintain consistency with the previous treatment of these payments.

National Network Roads Funding

As outlined in our submission in response to the Draft Report, Victoria considers that the capital component of National Network Road funding should be treated by inclusion. However, there are currently two Commonwealth Grant streams contributing to this funding: The Nation Building Programme (NBP) and Nation

Building Plan for the Future (NBPF). The nature of the projects funded and the source of funds for these grant streams makes it important that the Commission consider treating them differently.

The States partially fund National Network Road projects with State funding being assessed in the investment component of the capital assessment, recognising State disabilities; while the Commonwealth funding is being assessed APC. This seems incongruous, particularly when one considers that future maintenance of the same road will be assessed by applying disabilities in the Roads category. This leads to the same stretch of road being assessed in three different ways.

Infrastructure Funding

The Building Australia Fund (BAF) was set up as a one-off fund for major infrastructure projects such as the National Broadband Network. This funding pool resulted from an unprecedented period of economic growth and the consequent impact on Commonwealth budget surpluses. It is therefore unlikely to be recreated. The scale and timing of some of the projects funded from this source – including the Regional Rail Project for Victoria - is also extraordinary. Without this extraordinary funding source, projects of this scale may not have proceeded at all or may have been implemented over significantly longer time periods. Treating funding provided for such extraordinary projects by inclusion, thereby impacting on annual relativities in the short term would:

- (a) potentially have significant GST redistribution implications in the short term, despite the funding itself not impacting on States' underlying fiscal capacity or position in the short term; and
- (b) likely put delivery of the projects themselves at risk (which is clearly not the intended consequence of HFE).

The nature of infrastructure spending in general is that it is inherently 'lumpy' in that large projects arise periodically in different places. However, what distinguishes the NBPF is the extraordinary scale and one-off nature of the funding source. This is in contrast to the Nation Building Program (and the Auslink program which preceded it) which was an ongoing and relatively stable source of Commonwealth funding for national road and, more recently rail, projects. It could be argued that there are enough large road projects around the country to offset each other in terms of the GST distribution. Projects are continually starting and finishing, and contributing to the GST distribution to various degrees. In contrast, projects of scale such as the Victorian Regional Rail project are much less consistent in their timing and involve very large financial commitments when they do arise. This makes it unlikely that such projects will be occurring in several States simultaneously, thereby mitigating what would otherwise be a highly distortional impact on the Commission's calculations for distribution of the GST. The Regional Rail project in Victoria is a good example of such a large financial commitment; this project would not have proceeded without substantial Commonwealth funding.

Victoria therefore considers that Commonwealth funding for significant projects provided through the NBPF infrastructure projects should not affect relativities, to

ensure that such funding contributions do not compromise the underlying GST distribution in the short term. The underlying GST distribution should be determined by ongoing disabilities, not by temporary funding streams, even though such funding contributes to States' service delivery capacity over the very long term. As noted above, the NBPF comes from a one-off and temporary funding source that is unlikely to be repeated.

The possibility of losing hundreds of millions in GST funding could prejudice States to delay, or reduce the scope of, large infrastructure investment.