

**Response to Commonwealth Grants
Commission position paper 2008/30**

The Adjusted Budget

January 2009



Department of Treasury & Finance

Table of Contents

1. Introduction

1. Introduction	1
2. Capital assistance to GBEs	1
3. Reconciling to GFS Net Lending.....	1
4. Other issues.....	2
4.1 Currently excluded GFS transactions	2
4.2 Cross-subsidies within GBEs	2
4.3 General revenue assistance to local government.....	2
4.3.1 Northern Territory local government restructuring	2
4.4 Superannuation	3
4.5 Functional smoothing	3

1. Introduction

In commission position paper 2008/30, the CGC sets out the scope of the adjusted budget and requests State views on how various transactions should be treated by the Commission and how States currently treat a number of transactions in their own accounting frameworks.

Victoria's primary concern with the CGC's proposals in this paper is that the differing treatment of capital contributions to GBEs may lead to grant design impacts. In paper 2008/30, the Commission expresses the view that it will include transactions that contribute to the GFS net lending in the adjusted budget. The Commission does not intend to include capital injections to GBEs in the adjusted budget. This means that, to the extent States on average provide assistance to their GBEs through operating transactions, the amounts will be included in the adjusted budget. To the extent States provide this support through equity injections, it will not be recognised.

In Victoria's view, this provides an incentive for States to provide assistance (in particular, capital assistance) to GBEs through the operating statement rather than the balance sheet. This is discussed further in section 2.

2. Capital assistance to GBEs

There are two accepted methods of funding capital contributions by the General Government (GG) sector to the Public Non-Financial Corporation (PNFC) or GBE sector.

The first method, used by Victoria, involves the GG sector paying the PNFC's financing leases through the operating statement. This has no direct impact on the GG or PNFC's balance sheet. No assets or liabilities appear on the respective balance sheets and the PNFC's operating losses arising through use of the capital are funded by ongoing GG grants for the life of the assets. These grants fund interest costs and depreciation.

The second method is to provide capital through a direct balance sheet transaction. This transaction results in assets appearing on the PNFC's balance sheet, with an accompanying equity injection from the GG sector at the time of provision. Both the asset and the equity are reduced over time – the asset by depreciation, and the equity by operating losses, which are not offset by ongoing funding from the GG sector.

Under the CGC's proposal, Victoria considers there is an incentive for States to provide equity to PNFCs through the operating statement. CGC staff argued at the December 2008 meeting that all States will be treated as if they had the national average of both accounting treatments, and that this would prevent any grant design effects. Victoria is not convinced that averaging is a sufficient deterrent in this instance and asks that the Commission investigate further the impact of the differing treatments on the GST distribution.

3. Reconciling to GFS Net Lending

The CGC proposes to include a reconciliation term in its adjusted budget, called the Budget Balancing category. This category will contain net transactions that contribute to GFS net

lending but are excluded from or added to the adjusted budget (e.g. NCP payments and abolished State taxes). The category will be assessed EPC to ensure it has no impact on the GST relativities.

Victoria has no objection to the inclusion of the category. However, if it is to fulfil its purpose, the CGC must detail in its reports which items are included in the category and how they are calculated. If this is not done, the budget balancing category has the potential to create greater confusion than already exists. The category must also be genuinely EPC, unlike some other “EPC” categories that have common factors such as location or administrative scale applied to them.

4. Other issues

Currently excluded GFS transactions

Victoria is able to provide data on Assets Donated by function. Transactions relating to Land can be removed from assets donated. Assets Acquired below fair value can be provided as a total, but not by function. Victoria does not classify any transactions to Capital Revenue n.e.c.

Cross-subsidies within GBEs

Victoria currently does not have any cross-subsidies within GBEs or ‘reduced dividend’ requirements for GBEs.

General revenue assistance to local government

Victoria does record some payments to local governments (other than on-passing grants from the Commonwealth), although these are also recorded in “Grants and subsidies paid” in operating expense. These payments tend to relate to community-based programs that are better run by local governments, so they are probably different in nature to those mentioned by the Northern Territory.

4.3.1 Northern Territory local government restructuring

In Victoria’s view, payments to local governments to assist restructuring should be assessed (by the State government concerned) independent of the indigenous population or any other demographic group. Victoria fails to see how the demography of a local council or group of councils would influence how much it costs to restructure said council(s).

The decision to restructure local government in a State is generally based on financial considerations to make councils more financially viable and/or efficient. Victorian local government was restructured during the 1990’s with little or no financial compensation or assistance to local councils. The payment of compensation is a policy choice and should not enter into the CGC’s framework.

To the extent that the NT is using local government restructuring as a means of providing support to indigenous communities, this is not common policy across States and therefore should not be factored into the assessment.

Superannuation

The Commission proposes to apportion centrally held superannuation expenses, based on States' allocation of agency held superannuation expenses. Victoria apportions about 90 per cent of our centrally held superannuation expenses when advising the ABS of our GFS figures each year. The CGC proposes to allocate the remaining 10 per cent according to that pattern, which Victoria is comfortable with.

Functional smoothing

The Commission intends to discontinue functional smoothing in the 2010 Review. This is possible due to the use of more 2 and 3-digit GPC level expense data, which should be less volatile. Functional smoothing is currently carried out where the expenses have been classified to different GPCs from one year to the next. This often creates confusion when the adjusted budget is referred back to Sates for checking with the original data provided. Victoria fully supports the end of functional smoothing.