



ACT
Government

Chief Minister, Treasury and
Economic Development

Our File No: 2017/7177

Your File No:

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Commonwealth Grants Commission
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Michael

Dear Secretary

ACT Response to Commission Staff 2020 Review Draft Assessment Papers

I am pleased to forward to you the attached submission to the Commonwealth Grants Commission (Commission) 2020 Methodology Review of GST Revenue Sharing Relativities (2020 Review), as requested by email dated 20 April 2018 from Mr Marc Boisseau, Director, Transport and Welfare.

The submission responds to all 25 Commission Staff Draft Assessment Papers as well as the Commission Staff Research Paper CGC 2018-02-S *A broader assessment approach* and Commission Staff Discussion Paper CGC 2018-03-S *Draft 2020 Review Quality assurance strategic plan* and expresses in detail the ACT's positions on the Commission Staff proposals for the 2020 Review. The submission is a whole-of-government response to the papers that has been coordinated by the Chief Minister, Treasury and Economic Development Directorate.

The ACT notes that further submissions on the papers may be provided at a later date in order to capture the outcomes of the workplace discussions scheduled for 15-17 August, as well as any other supplementary material we consider would be helpful to the Commission. Chief among this material will be the provision of ACT data in relation to administrative scale and a comprehensive response to the Commission Staff positions on the national capital and cross border disabilities.

I would like to acknowledge the high quality of the papers and that while the ACT does not agree with all of the Commission Staff positions within them, we appreciate the clarity and depth to which they have been presented. This presentation has helped the ACT in identifying key issues and directing its response to the papers.

We look forward to continuing to work with the Commission in the progression of the 2020 Review and the ongoing implementation of Australia's system of horizontal fiscal equalisation.

Yours sincerely



David Nicol

Under Treasurer

31 July 2018



ACT
Government

**COMMONWEALTH GRANTS
COMMISSION 2020
METHODOLOGY REVIEW OF
GST REVENUE SHARING
RELATIVITIES**

DRAFT ASSESSMENT PAPERS

ACT Government submission

ACT GOVERNMENT SUBMISSION

JULY 2018

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CONTENT

ABBREVIATIONS	9
FOREWORD	15
INTRODUCTION	17
KEY POINTS	19
PART A.....	23
THE PRINCIPLE OF HORIZONTAL FISCAL EQUALISATION AND ITS IMPLEMENTATION.....	25
Summary	25
INTRODUCTION	25
THE OBJECTIVE OF HORIZONTAL FISCAL EQUALISATION.....	26
HORIZONTAL FISCAL EQUALISATION IN CONTEXT	26
SUPPORTING PRINCIPLES	27
What States Do	28
Policy Neutrality	29
Practicality	29
Contemporaneity	30
IMPLEMENTATION ISSUES	30
ASSESSMENT GUIDELINES.....	31
QUALITY ASSURANCE STRATEGIC PLAN	33
Summary	33
PART B.....	39
A BROADER ASSESSMENT APPROACH	41
Summary	41
INTRODUCTION.....	41
Measuring Revenue Capacity	42
Simplifying the Revenue Approach	43
Simplifying the Expense Approach.....	46

Commission’s Current Approach to Simplification.....	49
PART C	51
SPECIAL CIRCUMSTANCES OF THE AUSTRALIAN CAPITAL TERRITORY.....	53
Summary.....	53
INTRODUCTION.....	53
FOUNDATIONS OF THE AUSTRALIAN CAPITAL TERRITORY	54
CHARACTERISTICS OF THE AUSTRALIAN CAPITAL TERRITORY	54
Industry Characteristics of the Australian Capital Territory	56
Demographic Characteristics of the Australian Capital Territory	58
Employment and Earnings Profile of the Australian Capital Territory	59
Household Expenditure Characteristics of the Australian Capital Territory	61
Summary of Economic Characteristics of the Australian Capital Territory	61
Performance of the Australian Capital Territory Economy	62
IMPACT OF THE SPECIAL CHARACTERISTICS OF THE AUSTRALIAN CAPITAL TERRITORY ON HORIZONTAL FISCAL EQUALISATION	64
Role of the Commonwealth Grants Commission in Self-Government of the Australian Capital Territory.....	65
PART D	67
OVERVIEW OF THE DRAFT ASSESSMENT PAPERS.....	69
Summary.....	69
PROPOSED SCOPE OF ACTIVITIES AND ASSESSMENT STRUCTURE FOR THE 2020 REVIEW	69
PROPOSED DISABILITY ASSESSMENTS FOR THE 2020 REVIEW	69
REVENUE ASSESSMENTS	71
PAYROLL TAX.....	71
Summary.....	71
LAND REVENUE	78
Summary.....	78
STAMP DUTY ON CONVEYANCES	82
Summary.....	82

Scope of Assessment	83
Drivers of Revenue Capacity.....	84
Sale of Major State and Territory Assets.....	84
Elasticity Adjustment	86
INSURANCE TAX	87
Summary.....	87
MOTOR TAXES	89
Summary.....	89
GAMBLING TAXES.....	91
Summary.....	91
Gambling Taxation Assessment in the 2020 Review	92
MINING REVENUE	104
Summary.....	104
OTHER REVENUE	108
Summary.....	108
User Charges.....	109
COMMONWEALTH PAYMENTS.....	114
Summary.....	114
Needs Based Funding Models	116
Full or Partial Exclusion of Commonwealth Payments	118
Treatment of Financial Penalties.....	120
EXPENSE ASSESSMENTS.....	123
SCHOOLS EDUCATION.....	123
Summary.....	123
Specification of the Regression Model	125
User Charges.....	127
Commonwealth Funding of Government Schools.....	127
Commonwealth Funding of Non-government Schools	128
Data Source for Student Numbers	128
Students with Disabilities	128
Policy Effects on State and Territory Shares of Government and Non- government Students	129
Student Transport	130

POST-SECONDARY EDUCATION.....	131
Summary.....	131
HEALTH.....	135
Assessment Approach.....	135
Summary.....	135
Socio-demographic Composition.....	136
Remoteness and Service Delivery Scale.....	137
Substitutability.....	138
Cross-border Service Use.....	139
Non-hospital Patient Transport.....	140
Other Expenses.....	140
Component Expenses.....	141
User Charges.....	141
Assessment Structure.....	142
Cultural and Linguistic Diversity.....	142
WELFARE.....	144
Summary.....	144
Family and Child Services.....	146
Aged Care.....	147
Disability Services – National Disability Insurance Scheme.....	147
Disability Services – Non-National Disability Insurance Scheme.....	148
Concessions.....	148
Other General Welfare.....	149
User Charges.....	150
HOUSING.....	151
Summary.....	151
SERVICES TO COMMUNITIES.....	155
Summary.....	155
Utilities Subsidies.....	156
Community Development and Amenities.....	159
Protection of the Environment.....	160
User Charges.....	162
JUSTICE.....	164
Summary.....	164
Police Services.....	166

Courts	169
Prisons	172
User Charges	172
Other Issues	173
ROADS	174
Summary	174
TRANSPORT	180
Summary	180
Conceptual Case	183
Urban Transport Expenses and Infrastructure Models	185
Definition of Urban Areas	186
Non-urban Expenses	187
SERVICES TO INDUSTRY	188
Summary	188
Business Development Expenses	189
Regulation and Other Industry Support Services	190
Planning and Regulation for Major Infrastructure Projects	191
Other Research and Development Expenses	192
User Charges	192
Administrative Scale	193
OTHER EXPENSES	194
Summary	194
Natural Disaster Relief	195
Capital Grants to Local Government	196
National Parks and Wildlife Services	197
Cross-border Expenses	197
Administrative Scale	197
Other Issues Including Location	198
User Charges	198
PHYSICAL AND FINANCIAL ASSETS	199
Summary	199
Functionalising the Assessment	200
Refining the Assessment of Infrastructure Needs	201
Other Issues	202
Cost Factors	205

Presentation	205
DISABILITY ASSESSMENTS	207
WAGE COSTS	207
Summary	207
Other Issues Considered.....	208
GEOGRAPHY USED BY THE COMMISSION	213
Summary	213
Geography for Regional Costs Assessment.....	217
Broadening Evidence Base on Regional Costs.....	218
Measure of Indigenous Socio-economic Disadvantage	219
Other Issues Considered.....	219
ADMINISTRATIVE SCALE	221
Summary	221
Conceptual Case and Definition of Administrative Scale	223
Re-estimating Administrative Scale Costs.....	223
Adjustments for the Northern Territory and the Australian Capital Territory ..	224
Wages Costs Adjustment	226
Indexation of Administrative Scale Expenses.....	227
Presentation	227
OTHER DISABILITIES	228
National Capital.....	228
Summary	228
Cross-border	230
Native Title	232

ABBREVIATIONS

Term	Definition
ABC	Australian Broadcasting Corporation
ABF	Activity Based Funding
ABS	Australian Bureau of Statistics
ACARA	Australian Curriculum, Assessment and Reporting Authority
ACNC	Australian Charities and Not-for-profits Commission
ACT	Australian Capital Territory
ACTIA	ACT Insurance Authority
ACTPS	ACT Public Service
AFP	Australian Federal Police
AIATSIS	Australian Institute of Aboriginal and Torres Strait Islander Studies
AIHW	Australian Institute of Health and Welfare
AIRC	Australian Industrial Relations Commission
ALGA	Australian Local Government Association
ANF	Australian Nurses Federation
ANZSCO	Australian and New Zealand Standard Classification of Occupations
APC	Actual Per Capita
APRA	Australian Prudential Regulatory Authority
APS	Australian Public Service
ARIA	Accessibility/Remoteness Index of Australia
ASOL	Assessment System Online
Austrroads Standard	Austrroads Data Standard for Road Management and Investment Projects
BITRE	Bureau of Infrastructure, Transport and Regional Economics
CAEPR	Centre for Aboriginal Economic Policy Research
CALD	Cultural and Language Diversity
COAG	Council of Australian Governments

**ACT GOVERNMENT RESPONSE ON COMMONWEALTH GRANTS COMMISSION 2020
REVIEW DRAFT ASSESSMENT PAPERS**

CoE	Compensation of Employees
CoES	Characteristics of Employees
COFOG-A	Classification of the Functions of Government - Australia
Commission	Commonwealth Grants Commission
CoV	Coefficient of Variation
CSS	Commonwealth Superannuation Scheme
CTP	Compulsory Third Party
ED	Emergency Department
EGM	Electronic Gaming Machine
EMA	Emergency Management Australia
Employee expenses	Wages and benefits paid to employees by employers
EPC	Equal Per Capita
FAG	Financial Assistance Grant
FESL	Fire and Emergency Services Levy
FHOG	First Home Owner Grant
Gambling Research Report	Gambling Activity in Australia Research Report 2017
GBE	Government Business Enterprise
GDI	Gross Disposable Income
GDP	Gross Domestic Product
GFS	Government Finance Statistics
GHDI	Gross Household Disposable Income
GP	General Practice
GRA	General Revenue Assistance
GSP	Gross State Product
GST	Goods and Services Tax
HFE	Horizontal Fiscal Equalisation
HFI	Horizontal Fiscal Imbalance
HILDA	Household Income and Labour Dynamics in Australia

**ACT GOVERNMENT RESPONSE ON COMMONWEALTH GRANTS COMMISSION 2020
REVIEW DRAFT ASSESSMENT PAPERS**

ICSEA	Index of Community Socio-Educational Advantage
ICT	Information and Communications Technology
IGA-FFR	Intergovernmental Agreement on Federal Financial Relations
IHPA	Independent Hospital Pricing Authority
IRSD	Index of Relative Socio-economic Disadvantage
IRSEO	Indigenous Relative Socioeconomic Outcomes
MMM	Modified Monash Model
MSP	Municipal Service Grant
NAP	Non-admitted Patient
NCA	National Capital Authority
NCCD	Nationally Consistent Collection of Data on School Students with Disabilities
NCP	National Capital Plan
NCVER	National Centre for Vocational Education Research
NDIS	National Disability Insurance Scheme
NDRRA	Natural Disaster Relief and Recovery Arrangements
NEC	National Efficient Cost
NECR	Notional Employer Contribution Rate
NEP	National Efficient Price
NERA	National Education Reform Agreement
NHCDC	National Hospital Cost Data Collection
NHRA	National Health Reform Agreement
NISEIFA	Non-indigenous Socio-Economic Indexes for Areas
NNRA	National Network Rail
NNRO	National Network Road
NPP	National Partnership Payment
NRAS	National Rental Affordability Scheme
NSW	New South Wales
NT	Northern Territory

**ACT GOVERNMENT RESPONSE ON COMMONWEALTH GRANTS COMMISSION 2020
REVIEW DRAFT ASSESSMENT PAPERS**

NWAU	National Weighted Activity Unit
PATS	Patient Assisted Travel Schemes
PC	Productivity Commission
PNFC	Public Non-financial Corporation
PPP	Public Private Partnership
PSS	Public Sector Superannuation Scheme
QGSO	QLD Government Statistician's Office
QLD	Queensland
R&D	Research and Development
RAB	Regulated Asset Base
Review	Methodology Review of GST Revenue Sharing Relativities
ROGS	Report on Government Services
SA	South Australia
SA1	Statistical Area 1
SA2	Statistical Area 2
SDC	Socio-demographic Composition
SDS	Service Delivery Scale
SEIFA	Socio-economic Indexes for Areas
Service expenses	Operating costs net of depreciation
SES	Socio-economic Status
SFD	State Final Demand
SLGFCE	State and Local Government Final Consumption Expenditure
SPP	Specific Purpose Payment
SRS	Student Resource Standard
States	The states of Australia (NSW, VIC, QLD, WA, SA and TAS)
SUA	Significant Urban Area
TAS	Tasmania
Territories	The territories of Australia (ACT and NT)

**ACT GOVERNMENT RESPONSE ON COMMONWEALTH GRANTS COMMISSION 2020
REVIEW DRAFT ASSESSMENT PAPERS**

ToR	Terms of Reference
UCL	Urban Centre and Locality
Update	Update of GST Revenue Sharing Relativities
USA	United States of America
VET	Vocational Education and Training
VFI	Vertical Fiscal Imbalance
VIC	Victoria
WA	Western Australia
WPI	Wage Price Index

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FOREWORD

The ACT is committed to HFE as the ongoing basis for distributing the GST between the States and Territories into the future. The objective of ensuring that States and Territories have the fiscal capacity to provide the same standard of services is a key feature of the Australian economic and political landscape. The ACT considers that the current comprehensive system provides the best approach to achieving this objective.

The ACT is pleased that the Commission has affirmed this comprehensive approach, at least on an interim basis, for the purposes of the 2020 Review. This position is, of course, the subject of negotiations between the Commonwealth and the States and Territories following the Commonwealth's interim response to the PC's final report on its Inquiry into HFE. As this process is outside the current scope of the 2020 Review, we have prepared our submission on the basis of the continuation of the existing system. However, we note that supplementary ToR and further consultation will be required should any changes to the current arrangements be agreed.

The ACT acknowledges that with this comprehensive approach comes some complexity in the methodology and we generally support the Commission exploring alternative simpler methods. However, we agree with the conclusions of Commission staff that broader assessment approaches, while simpler, are not always consistent with the principle of HFE. We also oppose using materiality thresholds to lessen complexity as they reduce equalisation and transfer resources from the smaller to the larger jurisdictions. Instead the ACT proposes that materiality be redefined as a percentage, rather than a fixed dollar amount, to better reflect whether or not a factor is relevant for each individual jurisdiction.

The ACT supports the 2020 Review Quality Assurance Strategic Plan. This plan, developed jointly by the Commission and the States and Territories, ensures there are strategies in place that will result in reliable and accurate assessments of State and Territory fiscal capacities while also strengthening confidence in the processes undertaken to make these assessments.

Since the Commission's last visit to the ACT in 2008, the ACTPS has evolved into more streamlined Directorates under a *One Public Service* model, enhancing their capacity to provide effective and efficient management and reporting. This realignment has facilitated a whole-of-government approach to preparing the submission. In conjunction with all Directorates, the ACT's Chief Minister, Treasury and Economic Development Directorate has considered all 26 Draft Assessment Papers.

The ACT submission builds on our general support for the key issues raised in the Commission's Staff Draft Assessment Papers on the scope and structure, treatment of Commonwealth payments and assessments for the 2020 Review. However, we have a number of suggestions, aimed at improving the application of the principles of HFE, for consideration by the Commission. These suggestions range from presentational issues to improve transparency, such as incorporating user charges into specific assessments, to more fundamental changes to assessment approaches. For example, the submission proposes a framework and assessment for gambling taxes.

A key issue for the ACT is the proposal by Commission staff to cease all national capital planning allowances and reduce allowances for the impact of cross border utilisation of ACT Government services by non-residents.

**ACT GOVERNMENT RESPONSE ON COMMONWEALTH GRANTS COMMISSION 2020
REVIEW DRAFT ASSESSMENT PAPERS**

These allowances reflect the ongoing special circumstances of the ACT and are consistent with the application of the HFE principle that facilitated the successful entry of the ACT into the federation. We will provide further evidence to support our position in a supplementary submission later in 2018.

My thanks go to the Commission for the quality of the engagement to date and I look forward to the upcoming visit to the ACT. I also appreciate the efforts of all ACT Government officials involved in preparing this submission.

The ACT will continue to engage with Commission during the remainder of the 2020 Review both in responding to the issues as they arise from further work by the Commission and the States and Territories, as well as in providing additional evidence to support our positions.

I commend the submission to the Commission.

David Nicol
Under Treasurer
Chief Minister, Treasury and Economic Development Directorate
ACT Government
31 July 2018

INTRODUCTION

The ACT Government's ongoing involvement in the 2020 Review continues to be guided by the Commission's 2020 Review work plan. The 2020 Review work plan foreshadowed the release of the Commission Staff Draft Assessment Papers on all assessments to the States and Territories by the end of April 2018 with an invitation to submit comments with a response date of 31 August 2018. The Commission is required to produce a draft 2020 Review report in May 2019.

The 2020 Review Commission Staff Draft Assessment Papers, identifying the key issues for the assessments for comment from the States and Territories, comprise:

- An overview to the 2020 Review Commission Staff Draft Assessment Papers;
- 26 Commission Staff Draft Assessment Papers for each assessment and common disability factors;
- A research paper on a broader assessment approach; and
- A discussion paper on the quality assurance strategy.

In compiling the papers, we note that Commission staff have drawn on State and Territory views from the 2015 Review and preliminary work conducted during the course of 2016 and 2017.

This includes State and Territory comments in 2016 and 2017 on the Commission Staff Research Paper series *What States Do* and telepresence discussions during October and November 2017.

This early work proved to be very useful to the ACT in targeting the aspects of the existing methodology warranting closer scrutiny in the 2020 Review. The *What States Do* papers were particularly helpful and represented a major improvement on past Reviews. This submission draws on the specific issues raised for comment in each of the *What States Do* papers, underpinned by the ACT's own analysis of the proposed approaches, including identifying additional matters of concern to the ACT in a number of instances. The submission reflects a whole-of-government effort co-ordinated by the Chief Minister, Treasury and Economic Development Directorate.

In addition to the Draft Assessment Papers, the 2020 Review work plan also includes a Commission visit to each State and Territory in mid-2018. These visits are intended to build on the respective State and Territory submissions by providing an additional opportunity for the Commission and State and Territory officials to better understand each party's views and proposals. The ACT visit has been scheduled for 15 to 17 August 2018. The interplay between the submission, the Commission and staff and subsequent work place discussions is critical to the ACT's position within the context of the 2020 Review.

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KEY POINTS

This submission canvasses in detail the ACT's responses to the issues raised in the Draft Assessment Papers. In many cases, while we might agree with the Commission staff position, the submission expands on the rationale for our support. Likewise, the submission explains the reasoning for our disagreement with other Commission staff positions. Key messages from the submission are:

- The ACT agrees in principle with the stated interim Commission positions on the objective of HFE, the supporting principles and implementation guidelines for the 2020 Review.
- The ACT agrees to the Quality Assurance Strategic Plan, though we note that it is not always adhered to in practice and offer some suggestions for improvement.
- The ACT considers the Commission's current approach to assessing State and Territory fiscal capacities to be the best practice for achieving HFE, though we have concerns with the current implementation of materiality thresholds. We consider that materiality thresholds should be on a proportional, rather than absolute basis.
- The ACT does not agree with the view that the ACT Government could be expected to have matured sufficiently to adapt to the costs of the legacy of its physical, legal and institutional design and intends to provide more detailed evidence in a supplementary submission.
- The ACT supports the scope of State and Territory activities and disabilities and proposed assessment structure for the 2020 Review. We regard inter-Review consistency is essential and consider that Commission staff have struck the right balance.
- The ACT supports the Commission staff positions on the Payroll Tax assessment, though proposes an adjustment to improve the methodology by accounting for common payroll tax exemptions.
- The ACT supports the Commission staff positions on the Land Revenue assessment, though further proposes the discontinuation of assessing the revenue replacement amount associated with the ACT's tax reforms.
- The ACT supports the Commission staff positions on the Stamp Duty on Conveyances assessment, though proposes a differential assessment for revenue from the sale of major State and Territory assets.
- The ACT supports the Commission staff positions on the Insurance Tax assessment.
- The ACT supports the Commission staff positions on the Motor Taxes assessment.
- The ACT supports the Commission staff investigation into a differential assessment of Gambling Taxes and proposes a possible method to do so for the Commission's consideration.

- The ACT supports the Commission staff positions on the Mining Revenue assessment.
- The ACT supports the Commission staff positions on the Other Revenue assessment other than those for user charges. We describe three alternative options for assessing user charges.
- The ACT supports the treatment of needs-based Commonwealth funding on an EPC basis and EPC Commonwealth funding on a differential basis. However, we consider the treatment of Commonwealth infrastructure funding to be an area of significant weakness in achieving HFE that requires further consideration.
- The ACT broadly supports the Commission staff positions on the Schools Education assessment, though considers that student transport should be assessed in the Other Expenses assessment.
- The ACT supports the Commission staff proposals for the Post-secondary Education assessment.
- The ACT supports the Commission staff proposals for the Health assessment, while calling on the Commission to seek independent expert advice on substitutability rather than relying solely on State and Territory data.
- The ACT broadly agrees with the Commission staff proposals for the Welfare assessment. However, we request more analysis from the Commission staff on using low SES as a disability for assessing aged care and non-NDIS service expenses. Further we consider that Welfare user charges should be presented in the Welfare assessment and not in the Other Revenue assessment.
- The ACT is supportive of the Commission staff proposals for the Housing assessment.
- The ACT generally supports the Commission staff proposals for the Services to Communities assessment, though we express some concerns with the proposed treatment of utilities subsidies. We do not support assessing Protection of the Environment or non-indigenous development expenses in the Other Expenses assessment or assessing related user charges in the Other Revenue assessment.
- The ACT considers the Commission staff proposals for the Justice assessment to be reasonable, but considers that the assessment for corrective services should be discounted. We also consider that Justice user charges should be assessed in the Justice assessment and not the Other Revenue assessment.
- The ACT generally supports the Commission staff proposals for the Roads assessment, though we do not support distributing the other services component expenses of the assessment to the other components. We also do not support assessing Roads user charges in the Other Revenue assessment.

- The ACT does not support retaining the current approach to assessing urban and non-urban transport expenses. However, we agree with the Commission staff proposals on the definition of urban areas, inclusion of all SUAs in the assessment of urban transport and the criteria on which decisions to amalgamate satellite cities with their principal cities would be based.
- The ACT supports the Commission staff proposals for the Services to Industry assessment, though consider that a consistent approach to assessing R&D expenses should be adopted.
- The ACT does not support the Commission staff proposals on natural disaster relief expenses and national parks and wildlife expenses, though we do support the proposal to cease assessing grants to local government for community amenities and regional development.
- The ACT supports the structure of the Physical and Financial Assets assessment proposed by Commission staff, as well as Commission staff proposals on the treatment of investment generally. We do not support incorporating investment assessments into recurrent expense assessments.
- The ACT supports retaining the current methodology for the Wage Costs disability. We also reiterate our case for the reinstatement of the CSS disability and its expansion to include the PSS.
- The ACT considers that there are significant weaknesses in the SDS disability and support the Commission investigating merging the SDS and remoteness disabilities into a single disability. We also consider that SES should be assessed on individual-based measures rather than area-based measures. We otherwise support the Commission staff's proposed treatments of geography.
- The ACT supports the Commission staff efforts in re-estimating Administrative Scale expenses and the high level approach being taken by Commission staff. Our early view is that we have concerns with some of the estimates given by Commission staff.
- The ACT strongly opposes the dilution or removal of the disabilities for Cross-border and National Capital and notes we are currently preparing a comprehensive supplementary submission on these issues. We do, however, support the treatment of Native Title expenses on an APC basis, though propose that land rights expenses be assessed on the number of discrete aboriginal and Torres Strait islander languages in each State and Territory.

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PART A

STRUCTURE AND IMPLEMENTATION OF HORIZONTAL FISCAL EQUALISATION

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THE PRINCIPLE OF HORIZONTAL FISCAL EQUALISATION AND ITS IMPLEMENTATION

Summary

The ACT agrees in principle with the stated interim Commission positions on the objective of HFE, the supporting principles and guidelines and associated implementation issues for the remainder of the 2020 Review.

A key feature of the application of the HFE framework underpinned by agreed principles and associated guidelines, is that the Commission exercises judgment alongside its robust technical assessment process to deliver outcomes consistent with its observations and understanding of State and Territory circumstances.

INTRODUCTION

The Commission Position paper CGC 2017-21, *The principle of HFE and its implementation*, was released to the States and Territories in September 2017. The paper presents the Commission's interim positions on the objective of HFE, the supporting principles and guidelines and addresses associated implementation issues for the remainder of the 2020 Review. Commission staff have now sought views on this paper from the States and Territories as part of their responses to the Draft Assessment Papers.

The Commission paper was informed by an early round of consultations with the States and Territories, including Staff Discussion Paper CGC 2017-02-S, *The principle of HFE and its implementation*, released on 12 May 2017. The ACT Government responded to CGC 2017-02-S and participated in subsequent discussions between the Commission and the States and Territories in August 2017. The ACT is pleased that the Commission has accepted many of the positions we argued for as part of this consultation process.

States and Territories are responding to positions taken by the Commission and other States and Territories without a clear understanding of what the final HFE principles may be. This has made the progress of the 2020 Review for all parties, including the Commission and the ACT, much more uncertain and difficult.

Depending on the outcome of negotiations between the Commonwealth and the States and Territories it is possible that supplementary ToR will need to be issued to the Commission for the 2020 Review.

Given the parallel process of the PC Inquiry into HFE commissioned by the Commonwealth and the Commonwealth Government's response to it, the Commission has not been able to adopt a final position on the principles of HFE. In this context, the ACT welcomes the Commission indicating its intention to invite another round of submissions on the definition of HFE and its supporting principles and guidelines later in 2018, having regard to the outcome of the deliberations surrounding the Commonwealth Government's interim response to the PC's final report on HFE. Subject to further negotiations between the Commonwealth and the States and Territories, the ACT agrees in principle with the stated objective of HFE and the supporting principles outlined in CGC 2017-21. This support is discussed further below.

THE OBJECTIVE OF HORIZONTAL FISCAL EQUALISATION

As the ACT has consistently communicated, we continue to fully support the Commission's adoption of the current objective of HFE in the 2020 Review, namely that State and Territory governments should receive GST funding such that, after allowing for material factors affecting revenues and expenditures, each would have the fiscal capacity to provide services and the associated infrastructure at the same standard, if each made the same effort to raise revenue from its own sources and operated at the same level of efficiency.

With respect to the objective and definition of HFE, the Commission takes the view that the ToR are clear; it is to recommend how the GST should be distributed in accordance with the principle of HFE as understood and accepted by all governments when they signed the 1999 IGA-FFR and subsequent agreements.

Within the 2020 Review ToR, the Commission states it is not asked nor given the discretion to decide when other policy objectives or agreements between the Commonwealth and the States and Territories should moderate the achievement of HFE, nor is it given discretion as to which States and Territories the principle of HFE should be applied. The Commission therefore concluded it is not clear that achieving HFE can be made consistent with also facilitating other objectives, or at least minimising any perceived adverse impacts of HFE on the operations of government and the economy, in ways other than those dealt with by the supporting principles. Consequently, proposed GST distributions that advantage certain revenue bases over others (such as mining) or distributions based solely upon State and Territory population shares (as proposed by NSW) are not consistent with equalising State and Territory fiscal capacities; the goal the Commission has been set.

As required by its ToR, the Commission has also adopted the position that it must seek to deliver full equalisation to the closest degree possible, not partial equalisation. Accordingly, the Commission does not consider that discounting certain revenue bases or an EPC distribution of GST revenue would deliver HFE or be consistent with the Commission's ToR. Rather, such a distribution would exacerbate differences in fiscal capacity between the States and Territories and thus be likely to increase disparities in the provision of State and Territory services.

In summary, the Commission's view is that it must recommend a distribution of GST revenue on HFE grounds consistent with the IGA-FFR and its ToR. It intends to retain the definition of the HFE principle adopted in the 2015 Review as referenced above. Whether there are any changes to the ToR in response to the Commonwealth Government's interim response to the PC's final report on HFE will depend on further negotiations between the Commonwealth and the States and Territories.

HORIZONTAL FISCAL EQUALISATION IN CONTEXT

An understanding of what HFE is and its purpose in Australia's federal financial relations arrangements provides useful context to all parties when considering the Commission's approach to the task and views outlined in detail in this submission in relation to the 26 individual assessments.

The Commonwealth Government currently has the majority of taxation powers in Australia, while the States and Territories are responsible for the delivery of many high-cost services, including health (mainly public hospitals), education (mainly public schools), justice services, roads and public transport.

In addition to defence and customs, the Commonwealth also delivers most of the social assistance transfers (pensions, family allowances, Medicare payments and pharmaceutical benefits) and plays the major role in funding many service areas such as universities, child care and aged care. This revenue-expenditure imbalance (commonly referred to as VFI) is offset by significant fiscal transfers to the States and Territories from the Commonwealth Government, including the GST grant.

The GST is distributed among the States and Territories in accordance with the principle of HFE. HFE is the equalisation of the fiscal capacities of the States and Territories. This means each State and Territory receives sufficient GST such that it is capable of funding a quantity and quality of services and infrastructure equal to the national average, provided that it makes a national average effort to raise revenue from its own sources and operates at a national average level of efficiency. The GST that each State and Territory receives is thus dependent on material factors that affect its service delivery needs and costs and revenue raising capacity, as well as other grants from the Commonwealth.

HFE ensures that each State and Territory in Australia has the same fiscal capacity to deliver services. Each State and Territory may pursue its own policies and priorities, but its fiscal capacity to do so is equalised, taking account of the differences between jurisdictions in their tax bases and their service delivery needs or costs. In practice most of the spending by the States and Territories delivers a similar set of services across Australia. HFE makes this possible because each State and Territory has the same fiscal capacity.

Thus, HFE achieves outcomes that would otherwise require transfers of function to the Commonwealth. The payment of the GST as general revenue assistance in accordance with the principle of HFE allows State and Territory governments to deliver services according to their specific needs and circumstances. The combination of HFE and decentralised governance is a longstanding feature of the Australian Commonwealth (as well as many other federations).

Where equalisation is absent or limited, substantial differences in service levels or tax levels arise across sub-national jurisdictions, with substantial inequalities resulting from them.

This is evident in several federations, most notably the USA, although even then there is some equalisation, either through federally funded support programs in areas like schools, or through *ad hoc* spending proposals adopted through legislative processes.

SUPPORTING PRINCIPLES

The Commission has developed four supporting principles to guide its approach to achieving HFE, namely:

- *What States Do;*
- *Policy Neutrality;*
- *Practicality;* and
- *Contemporaneity.*

These principles are essential to the HFE framework and, while not universally accepted, are sound and should be seen as the building blocks to the HFE framework. The ACT supports these four principles in their entirety.

We do, however, propose some adjustments to the application of the principles, the ACT has no specific concerns with them. The most significant proposed changes relate to the *Policy Neutrality* principle which aim to strengthen the principle in three ways, as discussed later.

In regards to the ToR requirement for the Commission to consider whether different weights should be given to different supporting principles, the ACT accepts that, from an operational perspective, the interaction and subsequent friction between the supporting principles does require a balancing of competing considerations. This is particularly so when determining assessment methods. Hence, the ACT accepts the Commission decision to not establish any prior ranking or weighting of these supporting principles, contrary to the position in the ACT's response to Commission Staff Discussion Paper CGC 2017-02-S *The principle of HFE and its Implementation* which suggested *What States Do* and *Policy Neutrality* were a priority.

One of the most compelling and positive aspects of the application of the HFE framework is the fact the Commission itself retains the right to exercise judgment if its best endeavours to build a reliable assessment do not lead to an outcome consistent with its observations and understanding of State and Territory circumstances. The ACT remains fully supportive of this right, on the expectation that if the Commission were to deviate from the supporting principles, it will aim to clearly explain its reasoning.

Explanations of each of the four supporting principles and their purpose are provided below to facilitate an understanding for those parties viewing the ACT submission. The supporting principles, both individually and collectively, are essential to understanding how the Commission implements HFE. Additional ACT commentary is provided in some areas for clarity.

What States Do

The principle of *What States Do* is that the range of activities undertaken by the States and Territories should be reflected in the Commission's recommendations. It applies to deciding the scope of assessments and to identifying relative State and Territory needs.

It refers to what States and Territories collectively do (rather than what each does individually) because the assessment of fiscal capacity is based on determining what State and Territory revenues and expenditures would be under a common policy. The common policy assessed by the Commission generally is the (weighted) average policy of all States and Territories.

What States Do sets a factual standard, rather than an external judgment of what States and Territories should or could do. As the roles, functions, priorities and circumstances of the States and Territories change, so does the assessment of their fiscal capacities.

This is a fundamental pillar of HFE and must continue to be the very essence of how the Commission should approach the 2020 Review ToR.

The ACT has no further comments to add on the components of this principle, namely the scope of equalisation, weighted averages and average policy, internal standards and disability measurement to that already outlined in the ACT's response to Commission Staff Discussion Paper CGC 2017-02-S *The principle of HFE and its Implementation*.

Policy Neutrality

The principle of *Policy Neutrality* is that State and Territory policy choices should have minimal direct influence on HFE assessments and, conversely, that HFE should have minimal direct influence on State and Territory policy choices.

HFE has the potential to interact with policy choices, but this can be mitigated through assessing fiscal capacity on the basis of the weighted average of the policies of the States and Territories. In most cases, each State and Territory has only a small influence on the average policy of all States and Territories. However, exceptions can arise. For example, over the past decade *Policy Neutrality* has been of particular concern in the assessment of State and Territory mining revenues. Commission staff aim to modify the assessments in such circumstances to maximise *Policy Neutrality*.

One such proposed modification is to ensure that future discretionary revenue policy changes do not excessively change the GST distribution. It will do this by limiting the extent to which any discretionary change in mineral royalty rates by a State or Territory flows through to the assessed revenue capacity of that State or Territory. The result generally will be that States and Territories will retain at least half of the own-source revenue effects of its royalty rate change.

The Commission will also aim to strengthen the application of *Policy Neutrality* in two further ways. It will aim to ensure that assessments do not unduly reward States and Territories which place moratoriums or bans on mineral and energy developments (for example, coal seam gas production). The Commission is also undertaking a consultancy exploring adjustments to revenue assessments that will minimise, to the extent practicable, tax reform disincentives arising from the effects on tax bases of tax policy choices (tax elasticity).

The ACT offers its full support for the proposed Commission actions to strengthen the application of *Policy Neutrality*. The Commission consultancy on tax elasticity effects is particularly welcomed.

This latter point is highly relevant to the ACT given its tax reform agenda and was a major focus in earlier ACT submissions to the 2020 Review process.

Tax elasticity will be subject to further discussion and possible submissions beyond the bounds of this submission and the upcoming workplace discussions later in 2018.

Practicality

The principle of *Practicality* is that assessments should be based on sound and reliable data and methods and be as simple as possible, while also reflecting the major influences on State and Territory expenses and revenues.

The Commission has decided to add a further element to the practicality principle, namely 'fitness for purpose'. States and Territories have emphasised to the Commission their need for transparent, reliable and, where possible, reasonably predictable relativities in time for their State and Territory budgets.

The Commission therefore intends that this principle also support methods that provide relativities that are practical for States and Territories to incorporate into their budget management processes.

The ACT agrees with the general thrust on the elements of this principle, namely simplicity, reliability, materiality, quality assurance and fitness for purpose. However, we have concerns regarding the implementation of two of these items; simplicity and materiality, which are discussed later.

Contemporaneity

The principle of *Contemporaneity* is that the Commission should seek to minimise the lag between the years in which reliable data are available to make an assessment (the assessment period) and the year in which the resulting relativities will be applied (the application year). Since 2010, the assessment period has been the three most recently ended financial years. This amounts to using the three financial years that are two to four years before the application year (e.g. the assessment years for the 2018 Update, which applies for 2018-19, were 2014-15, 2015-16 and 2016-17).

Most States and Territories support the current approach, on the basis that it provides greater predictability of GST shares and hence assists with their budget management. Notwithstanding this, the Commission has not settled on whether the size of the assessment window should be changed and will give further consideration over the course of the 2020 Review as to whether there should be one, two or three assessment years.

Conversely, the ACT argued in its response to Commission Staff Discussion Paper CGC 2017-02-S *The principle of HFE and its Implementation* in favour of replacing data from the earliest assessment year (e.g. 2014-15 for the 2018 Update) with estimated outcomes for the pre-application year (e.g. 2017-18 for the 2018 Update). This proposal is on the basis that it would improve State and Territory fiscal and economic management through improved *Contemporaneity*.

However, the Commission indicated it is not attracted to using State and Territory or independent estimates of revenues in the pre-application year, on the basis that they are unlikely to be sufficiently reliable for use as the basis of the GST distribution. The ACT sees no further value in pursuing the matter until (and if) the Commission presents an alternative. The current approach is supported by the majority of jurisdictions, hence the ACT reserves its position on *Contemporaneity*.

Contemporaneity was also addressed in the PC Inquiry into HFE final report.

IMPLEMENTATION ISSUES

A number of other issues arise from the implementation of the supporting principles warranting further consideration.

Implementation issues are always subject to much discussion but are not viewed as principles of HFE in and of themselves. Rather, they are matters relating to the simplification of the assessments and ensuring consistency in the treatment of Commonwealth Government grant funding to the States and Territories.

Firstly, the Commission intends retaining its current guidelines for the assessment of Commonwealth Government payments to the States and Territories.

Specifically, payments which support State and Territory services and for which expenditure needs are assessed, will affect GST shares. The ACT fully supports this approach.

Secondly, in support of simplification, the Commission has indicated it will continue to assess State and Territory needs only where doing so makes a material difference to the distribution of GST revenue for any State or Territory. The Commission intends to increase the materiality threshold to account for price and wages increases. The proposed materiality threshold for a disability is \$35 per capita (an increase of \$5 since the 2015 Review) while the threshold for data adjustments is proposed to remain at \$10 per capita.

The Commission will also continue its current approach of discounting its measurement of disabilities where there are substantive concerns about data quality. Three levels of discount may be applied – low (12.5 per cent), medium (25 per cent) and high (50 per cent) – depending on the Commission’s judgment about the reliability of the data for the purposes of the assessment.

While the Commission considers that maintaining materiality thresholds is an effective way of maintaining simplicity in its assessments and to ensure that attention is focused on the major drivers of differences between the States and Territories, the ACT has consistently argued otherwise. Similarly, some States and Territories, including the ACT, have concerns regarding the appropriateness of having discounts and with the consistency of their application. It is understood these issues will be considered as they arise over the course of the 2020 Review as assessments are developed further. This submission highlights the areas of most concern to the ACT.

The ACT has no particular concerns with other implementation issues raised, including quality assurance, backcasting and the treatment of Commonwealth Government payments to the States and Territories (with the exception of those for NNROs and NNRA, which are elaborated upon in the Commonwealth Payments section of the submission).

ASSESSMENT GUIDELINES

The ACT notes and agrees with the Commission intention to maintain the assessment guidelines developed in the 2015 Review for the 2020 Review. The guidelines allow the Commission to give effect to the HFE objective having regard to the supporting principles. They have been developed in consultation with the States and Territories and cover the steps for establishing and measuring disabilities, when and how discounting decisions are made and applied and the threshold for recognising a disability.

The guidelines also form a key part of the quality assurance process. They allow the Commission to be confident all relevant steps in the decision-making process are followed. They allow external parties to follow the Commission’s decision processes and to form conclusions about whether due process has been observed.

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QUALITY ASSURANCE STRATEGIC PLAN

Summary

The ACT is cognisant of the 2020 Review ToR requirement for the Commission to implement a robust Quality Assurance Strategic Plan underpinning its assessments and most importantly, the recommendations for the 2020 Review. The ACT considers there to be five main factors relevant to any such plan:

- Transparent assessment guidelines;
- Reliable and high quality data and evidence;
- Use of external inputs;
- Documentation of inputs and outputs; and
- Endorsement of outputs.

These processes, however, are not always fully adhered to in practice, leading to some gaps in their coverage and/or application. This has occurred in a number of recent Updates, with the ACT experiencing large and uncommunicated data revisions resulting in negative material impacts on its GST share. The ACT considers that four key messages can be taken from these experiences which should be better reflected in the plan:

- Open consultation and sharing of drafts in advance of publication should occur if the opportunity exists;
- An adequate timeframe to review the Commission reports while under embargo is required;
- The Commission staff should alert jurisdictions to any known material data adjustments in advance of the release of any Update or Review Report; and
- A more proactive approach being adopted by the Commission in educating the community about HFE.

The ACT is cognisant of the 2020 Review ToR requirement for the Commission to implement a robust Quality Assurance Strategic Plan underpinning its assessments and most importantly, the recommendations for the 2020 Review. The plan entails a program that facilitates a link between the current and past quality assurance protocols, thereby ensuring an incremental improvement of the assessments between Reviews and the ability for the assessments to be updated during annual Updates.

This ongoing quality assurance underpinning the work of the Commission in consultation with the States and Territories dates back to the 2010 Review and was continued in the 2015 Review. The ACT Government recalls initial work was done as early as 2005 in conjunction with the States and Territories. In addition, achieving improvements in the quality and fitness for purpose of both data and methods is paramount. Equally important is the confidence of the States and Territories in the final recommendations.

The ACT considers there to be five main factors relevant to any such plan:

- Transparent assessment guidelines;
 - The development and implementation of the assessment guidelines driving the 2020 Review is crucial to improving the reliability and transparency of the Commission's work and strengthening the acceptability of equalisation. The guidelines are vital to the Commission's quality assurance process. They should provide a structured and consistent approach to decision making that builds in benchmarks and criteria that must be met before assessments are made. The Commission addressed this matter early in the 2020 Review.
- Reliable and high quality data and evidence;
 - The quality and reliability of evidence and data that enter the decision making and calculation processes are vital to the quality of the Commission's recommendations. Improving the reliability of methods provide for better-targeted evidence from the States and Territories by making it clear that arguments for new assessments or the continuation of existing ones must meet the benchmark standards of materiality and reliability before they are accepted. The Commission continues to apply this requirement as part of the 2020 Review.
- Use of external inputs;
 - The Commission's work has been criticised on the basis of its complexity and the limited number of people from the Commonwealth and State and Territory Governments who are involved in the development and evaluation of its methods. As part of the processes for increasing the reliability and transparency of HFE, the Commission and the States and Territories continue to agree on the need for external expert assistance in the development and review of methods in important areas.
- Documentation of inputs and outputs; and
 - The Commission continues to provide extensive documentation of its processes and methods through its reports, supporting documents and working papers, with all material being published on its website since 1999 when the website was established. Submissions by States and Territories and other parties are also published if approval is received from them to do so. However, despite the extent of the documentation and ongoing efforts to improve its quality and accessibility, improvements could always be made, such as more clearly identifying the reasons for decisions and judgments. The ACT Government suggests that improving the accessibility of ASOL be examined, including exploring moving ASOL onto the Commonwealth Grants Commission Cloud, improving the accessibility and security of the system and options for more flexible and user friendly forms of data presentation.
- Endorsement of outputs.
 - The draft strategic plan requires verification to the Commission and external parties that quality assurance processes are in place and have been applied. This will partially be done through improved performance reporting by the Commission and its staff, especially the increased transparency and documentation of decision making processes and reasons for decisions and judgments.

- However, as acknowledged in the draft plan, it will also require external evaluation of the processes and their application. The involvement of external experts in the development of the strategic plan is welcomed.

In that context, the ACT is confident the draft 2020 Review Quality Assurance Strategic Plan will address these five factors. Indeed, if fully implemented, the Commission will achieve further outcomes also considered important by the ACT Government, namely:

- A balanced approach to past Reviews and the 2020 Review;
- A program of continuous improvement of the assessments;
- Increased level of transparency of changes; and
- Maintenance of a degree of simplicity as best can be achieved in a highly complex area of public policy.

These processes, however, are not always fully adhered to in practice, leading to some gaps in their coverage and/or application. This has occurred in a number of recent Updates, with the ACT experiencing large and uncommunicated data revisions resulting in negative material impacts on its GST share.

While these matters have been documented with the Commission in their post-Update report processes under the auspices of the Quality Assurance Strategic Plan, four key messages can be taken from these experiences which the ACT considers should be more reflected in the plan.

The ACT had concerns that two of its positions were not adequately reflected in the 2018 Update report. The Secretary of the Commission subsequently addressed the ACT's concerns, noting that both parties considered the matters more about interpretation rather than fundamental errors which might have impacted on the recommendations. While the ACT accepted this point, we note that there was no opportunity to provide clarification prior to the release of the report.

Based on these experiences, the first key message is that open consultation and sharing of drafts in advance of publication should occur if the opportunity exists. This would recognise that the complexity of many assessment issues presents Commission staff with a difficult task in attempting to fairly represent State and Territory views in the form of a short summary based on, at times, extensive State and Territory comments.

The second message is that an adequate timeframe to review the Commission Reports while under embargo is required. Given that this timing is determined by the Commonwealth, it would be beneficial for all jurisdictions to provide feedback directly to the Commonwealth Treasury of a collective concern about arrangements for recent Updates and Reviews.

This latter matter is referred to in the objectives of the Quality Assurance Strategic Plan, (Paragraph 9) which states:

“In 2006, Heads of Treasuries developed a protocol governing what should occur when States provide data (including revisions) late in the update process or if errors are found in the Commission’s recommendations.

It is a matter for heads of Treasuries to consider whether that protocol remains appropriate to current needs and practices or could be updated”.

The ACT would welcome this matter to be elevated to the Council on Federal Financial Relations with the support of the Commission.

Of greater concern to the ACT, however, was the estimated loss of \$44 million in GST to the ACT in the 2018 Update through the Payroll Tax assessment due to revisions of ABS payroll data. The Payroll Tax assessment had been a source of large data revisions in three of the last four Updates/Reviews, with no warning which could have given the ACT time to examine the reasons for the revisions or to prepare for their impact on the ACT’s relativity.

The ACT was under the impression, following an error in ABS data in the preparation of the 2015 Review, that it would be alerted in advance to any material data adjustment. Unfortunately this did not occur. Commission staff had been assured of the accuracy of the data by ABS staff. The ACT followed up the matter with the ABS. Although it appears that there was no error in the ABS data provided for the 2018 Update, the degree of volatility in the ACT’s data over recent years is an ongoing concern that has not been satisfactorily addressed.

Thus, the third key message is that the Commission staff, within the context of the Quality Assurance Strategic Plan, should exercise a higher degree of judgement in alerting jurisdictions to any known material data adjustments in advance of the release of any Update or Review Report.

The last remaining area of comment is on the public debate on the principle of HFE. Objective Two of the Quality Assurance Strategic Plan states:

“The Commission will provide different types and levels of information on its website for other audiences, to promote better understanding of equalisation and the work of the Commission”.

Many commentators, including the PC in its inquiry into HFE, have remarked that the Commission, through its Chairperson and Commission members, should provide a strong neutral voice in the public discussion of the HFE system. The Commission historically has viewed that supporting the architecture of the HFE system has been a role for governments, with its role being to operationalise the system as defined in ToR. The Commission has not seen its role as being to educate the public about HFE.

The ACT does not necessarily disagree with the Commission’s position. However, a fourth key message is that the ACT would support a more proactive approach being adopted by the Commission educating the community about HFE.

A proactive educational program on the HFE framework, how it is constructed and its results may be implemented by adopting a more visible public profile, including media statements and other correspondence during the release of major reports and briefings to elected representatives of the Commonwealth and State and Territory Governments. In effect, the ACT supports increased interactions between the Commission and organisations and individuals not directly involved in its inquiries, such as academic, government, media and special interest groups. Such interactions would better inform the public debate on the role of the Commission and the application of HFE.

**ACT GOVERNMENT RESPONSE ON COMMONWEALTH GRANTS COMMISSION 2020
REVIEW DRAFT ASSESSMENT PAPERS**

Simply placing material on a public website should not be seen as sufficiently achieving Objective Two of the Quality Assurance Strategic Plan.

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PART B

COMMONWEALTH GRANTS COMMISSION STAFF RESEARCH PAPER – A BROADER ASSESSMENT APPROACH

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A BROADER ASSESSMENT APPROACH

Summary

Australia's system of HFE has been lauded for being the most comprehensive system of equalisation practised anywhere in the world. However, with that comprehensiveness comes some complexity which has led to criticism of the system. In response to these critiques, the Commission has, on numerous occasions, explored alternative simpler approaches to assessing State and Territory fiscal capacities.

The ACT is supportive in principle of the exploration of alternative simpler means to assess State and Territory revenue raising capacity and expense needs, but we note that simplicity is not a prerequisite of an effective HFE system. We regard the objective of HFE of ensuring that States have the fiscal capacity to provide equivalent services of equal quality to be the key criterion for measuring the efficacy of alternative assessment approaches. It is our view that simplicity and stability are secondary considerations to equity.

With that in mind, the ACT considers the alternative assessment approaches explored by Commission staff to simplify the process do not achieve the overarching objective of HFE for a range of reasons. These reasons include the proposals not accounting for the different composition and distribution of otherwise equivalent tax bases across States and Territories, the inability of States and Territories to access the tax bases utilised by the Commonwealth, the generation of inequitable outcomes contrary to the objective of HFE and the lack of available data.

We also have some concerns with the manner in which the Commission is currently attempting to simplify its assessments, specifically the use and proposed increase of materiality thresholds. We note that the current practice of using absolute materiality thresholds results in more components being considered immaterial the more disaggregated an assessment becomes. Related to this, the ACT strongly opposes increases to materiality thresholds, as we consider they detract from the achievement of the objective of HFE.

The ACT proposes an alternative of using a proportion (e.g. five per cent, 10 per cent) of the dollar amount in an assessment, or component of an assessment, which is redistributed as the minimum threshold.

INTRODUCTION

The Commission has been criticised for having assessment methods that are too complex; consequently, Commission staff have explored other approaches to measuring States' and Territories' expenditure requirements and revenue capacity. Most research in this area has focussed on approaches to revenue capacity rather than expenditure requirement. The key question which the Commission is seeking to answer is whether it is possible to find alternative expense and revenue approaches that:

- Could be combined into an integrated approach to measuring States' and Territories' fiscal capacity; and

- Are consistent with the equalisation principle.

Measuring Revenue Capacity

Context

At the time comprehensive equalisation was first introduced (1981 Review), the Commission made a decision between two principal approaches to equalisation of revenue:

- A global approach – based on a general measure of revenue capacity; and
- A tax approach – based on the revenue bases on which State and Territory taxes were actually imposed.

The Commission chose the tax approach because the implied differences in taxable capacity under the global approach would be substantially less than the aggregated differences in the capacity of States and Territories to raise revenue from the individual taxes which they actually levied. Application of a global approach would have reduced the degree of equalisation through Commonwealth grants and required States and Territories with lower taxable capacity in relation to individual taxes to levy taxes and charges at higher rates than States and Territories with higher capacity, in order to raise the same per capita revenue. The tax approach, by contrast, is much more closely related to what States and Territories actually do.

States and Territories supporting a global approach in previous Reviews, such as NSW and WA, have argued that such an approach would be less policy influenced, simpler and likely to produce more stable GST outcomes than the current methodology.

Commission Staff Position

Commission staff explored alternative approaches to assessing revenue capacity in their May 2017 Research Paper 2017-03 *Achieving HFE – Other Approaches to Distributing the GST*. It canvassed two options:

- A global approach – a single broad assessment of all revenue streams.
- A macro approach – a broader assessment of each revenue stream.

The global approach involved using GSP as the single measure driving the assessment of all State and Territory revenue streams.

The macro approach involved using a single measure for each revenue stream (assessment), rather than breaking assessments down into components which could have separate measures e.g. Land Revenue capacity was measured by value of land; motor vehicle registrations by number of vehicles.

ACT Position

The ACT supports the investigation of alternative options for the assessment of revenue, but considers that evaluation of these options must give first priority to the fundamental objective of HFE, with simplicity and stability being secondary considerations.

Simplifying the Revenue Approach

Context

There is general acceptance among States and Territories that differences in the value of economic activity or assets, such as value of payrolls, value of land, value of property transferred and value of mineral endowments, should affect States' and Territories' assessed revenue capacities. However, there is disagreement over whether their assessed capacities should be affected by their collective policies on:

- The parts of the activity they tax (for example, the use of exemptions and tax free thresholds); and
- The rates of tax applied to various parts of the activity (for example, the use of concessions and progressive rates of tax).

In this light, States and Territories with the same total value of a given tax base may in practice have a different capacity because of the differing distribution of the base over its components or its range of values. The approach currently adopted by the Commission takes account of State and Territory differences in exemptions, thresholds, concessions and progressive rates, by using weighted averages and other adjustments to produce a common basis of assessment across all States and Territories.

The current approach of the Commission contrasts with a macro approach, which would make no such adjustments, simply making an assessment of revenue using the total value of a tax base, ignoring its distribution or composition.

Commission Staff Position

Macro Approach

Commission staff characterise the macro approach as putting less weight on the *What States Do* supporting principle and more on the *Policy Neutrality* supporting principle than the current approach.

One of the reasons the Commission has followed the adjustment approach to assessable tax bases is because it has a counterpart on the expense side, which recognises that some States and Territories do not provide services to some groups of people or that some groups cost more to service than others. Adoption of a macro approach to revenue assessment would imply adoption of a comparable approach to expense assessment.

Global Approach

Commission staff also note that a global approach would mean that States' and Territories' revenue capacity would not be related to the value of economic activity or assets in particular segments of their economies, but to a broad measure of activity or assets across their entire economies. A similar approach could be taken in relation to expense assessment.

ACT Position

Macro Approach

The macro approach has some merit in terms of simplification, by eliminating specific adjustments to allow for State and Territory differences in exemptions, thresholds, concessions and progressive rates of tax.

This also reduces the impact of State and Territory policy differences. However, its practical implication, as shown by Table 2 (p.8) of the Draft Assessment Paper, is a major redistribution of GST, around \$480m, away from the smaller States and Territories and towards the larger States.

A key consideration is the failure of this approach to take account of the different composition and distribution of otherwise equivalent tax bases across States and Territories. A good example is property values, where the smaller States and Territories lack the very high value properties found in the larger States – this clearly reduces the relative ability of the former to raise revenue from this base. The assumption of flat rates of taxation across tax bases, with no thresholds or exemptions, does not recognise differing capacity of taxpayers across States and Territories to pay and hence differing capacity of States and Territories to raise.

Global Approach

The Commission's current assessment approach focuses on legal tax bases rather than underlying economic capacity of States and Territories. An alternative approach based on global indicators of fiscal capacity would have substantial benefits in terms of simplicity, particularly on the revenue side of assessments. However, a critical issue is whether States and Territories can effectively access taxable capacity in alternative ways where they do not have the legal (or de facto) capacity to tax certain bases.

The assumption underlying the global indicators approach is that high-level economic indicators such as GSP and GDI are a good measure of States' and Territories' fiscal capacity. However, although such measures give a good impression of States' and Territories' overall economic strength, they are not necessarily an accurate reflection of the fiscal capacity of State and Territory governments. This is caused by two factors; VFI and HFI.

VFI means that many large and efficient tax bases are not available to States and Territories. Income, consumption and excise taxes are legally (or effectively in practice) reserved to the Commonwealth. The two large efficient (or potentially efficient) tax bases available to States and Territories are payroll tax and land tax.

Conveyance duty is also a major State and Territory revenue source but is a highly inefficient tax – for purposes of this analysis, it is assumed that conveyance duty is replaced by broad-based land tax on a revenue neutral basis. In 2015-16, these State and Territory tax bases generated revenue of \$22.5 billion for payroll tax and \$33.4 billion for land tax. By contrast, in 2015-16 the Commonwealth's revenue from personal income tax was \$187.1 billion, from corporate income tax \$62.9 billion and from excise and customs duties \$35.4 billion; while consumption tax (GST) generated \$57.5 billion. Clearly, the Commonwealth government has access to much broader tax bases than the States and Territories in aggregate.

This imbalance on its own would not be a problem for distribution of the GST under a global indicators approach if States' and Territories' fiscal capacities were closely aligned with the broader capacities of their economies. However, that is not the case, in particular due to the very uneven distribution of mineral resources across States and Territories. Although mining revenue constitutes only about seven per cent of all State and Territory own-source revenue, it is responsible for a larger amount of redistribution of GST than any other revenue or expenditure assessment. WA collected 55 per cent of all mining revenue in 2015-16, with QLD collecting another 25 per cent and NSW about 14 per cent; the remaining States and Territories collecting only six per cent of the total national revenue between them.

The ACT represents another illustration of this problem, on a much smaller scale, because of the legal barrier to States and Territories applying payroll and land taxes to the Commonwealth. This has a disproportionate impact on the ACT compared with the States and the NT.

The inability of State and Territory governments to access the broader tax bases available to the Commonwealth means that they cannot “get around” the problem of misalignment of their fiscal capacity with their broader economic bases, at least as far as revenue is concerned. There is even less scope to remedy the problem on the expenditure side, given the persistent nature of SDC which is a key driver of different expenditure needs between States and Territories. Thus, it is the interaction of VFI and HFI that makes broad indicators a poor alternative to the Commission’s current methodology focused on the legal tax bases available to States and Territories. The only way in which broad indicators could be made a workable alternative would be under a fundamental reform of the Federation, both in terms of taxation powers and expenditure responsibilities, which could bring States’ and Territories’ fiscal capacity into alignment with their broader economic capacity.

The practical deficiencies of a broad indicators approach are illustrated by of the PC’s Draft Report on HFE, October 2017 (see Tables C.9 and C.10, pp.232-233). These tables show negative relativities for the ACT and NT on some indicators, which implies that the Territories would not only receive no GST payments at all, but would also need to provide some of their own revenue to distribute to the States. Even the less drastic indicators would cause a decline in the ACT’s relativity to levels below the lowest level experienced by WA in recent years.

The key reason why the fiscal capacity of the ACT is far below that suggested by the broad indicators of GSP and GDI is the inability of States and Territories to apply payroll tax to Commonwealth employment. The very large role of the Commonwealth government in the ACT economy means this negative impact on the potential revenue base is far larger in the ACT than in the States and the NT. If the ACT were able to apply payroll tax to Commonwealth employment, it would become a significant net GST donor on an ongoing basis. Furthermore, there is no reasonably equivalent tax base which the ACT could levy to obtain equivalent revenue to payroll tax on the Commonwealth (i.e. of similar scope and incidence to payroll tax).

This could only be the case if the ACT was able to levy an income tax or consumption tax on its residents – however, these are Commonwealth taxes which are not available to States and Territories. A broad-based land tax (general rates in the ACT) does not qualify as such a tax given the burden falls solely on landowners. Box 1 of the Staff Research Paper (p.11) neatly summarises the ACT’s revenue capacity problem.

Commission staff have also provided a comparison of the tax approach with a range of global measures, including GSP, partial GSP, total factor income, GHDI and household final consumption expenditure. These comparisons show drastic redistributive effects between States and Territories in moving away from a tax approach to a global measures approach, in particular redistributing GST away from the smaller States and Territories and towards the two big resource States (WA and QLD).

A global approach based on GSP would redistribute \$2.2 billion in GST from the smaller States and Territories, with QLD gaining about \$1.4 billion.

The ACT supports the conclusions of a previous Commission and of Commission staff in this latest paper, that a global approach would overestimate the fiscal capacity of the weaker States and Territories and underestimate that of the strong, forcing weaker States and Territories to either impose taxes and charges at rates above those of the strong States, or reduce their services to a level below that of the strong States. Such outcomes would be inconsistent with the equalisation principle, which is the primary and overriding consideration in the Commission's deliberations.

Simplifying the Expense Approach

Context

In contrast with revenue assessments, little attention has been devoted to options for broad simplification of expense assessments, despite the fact that the latter are far more numerous and complex. States which have advocated for broader approaches to revenue assessments have not addressed the application of such approaches to expense assessments, perhaps because of likely offsetting losses they would incur if the Commission adopted a symmetrical position on the issue.

Commission staff have investigated options to simplify State and Territory expense assessments based on:

- A subset of the existing expense assessments;
- A subset of State and Territory attributes;
- Regressions of State and Territory actual spending;
- National government expenses; or
- Past expense assessments.

Indicators such as national government expenses and past assessed expenses are seen by the Commission staff as similar to the use of GSP as a measure of underlying revenue capacity.

Commission Staff Position

Subset of Existing Expense Assessments

Commission staff used a regression analysis to identify the subset of existing assessments that were the best explanatory variables for total assessed expenses and the weights which would need to apply to those assessments if they were to be used as the basis of a simplified global expense assessment.

This option was found to produce similar GST outcomes to the current approach, with only half of the existing assessments required. However, this reduction did not involve an equivalent gain in simplification.

A variant of this option was also canvassed, involving extrapolating from the four largest expense assessments. This option produced much bigger GST changes, with a major negative impact on the small jurisdictions, particularly TAS and the ACT.

Subset of State and Territory Attributes

Commission staff used regression analysis to identify a subset of State and Territory attributes (drivers) and associated weights which could provide a reasonable approximation of the existing expense approach, recognising that there are a number of common drivers across expense assessments. The selected attributes were indigeneity, remoteness, age over 65 and population growth.

This approach produced large GST effects compared with the existing approach, with the smaller States and Territories generally being big losers from this approach. This option would also require periodic updating of the weights to reflect changes in State and Territory circumstance and policies. The Draft Assessment Paper notes that there are no existing national data sets which could be used to generate weights for attributes other than indigeneity, implying a continuation of the type of data collection and analysis underlying the existing approach.

Regressions of State and Territory Actual Spending

Another option canvassed by Commission staff was the use of regression analysis of actual State and Territory spending against selected State and Territory attributes considered to be policy neutral. This approach is limited by the small number of States and Territories in Australia, which in turn limits the number of data points and thus the robustness of the analysis. The use of data from more than one year was also seen as possibly problematic in terms of independence of data across years.

National Government Expenses

This option is based on the premise that differing per capita expenditure across States and Territories by the Commonwealth Government, which is based on nationally consistent priorities, could provide a good indicator of relative expense needs of States and Territories. However, as noted in the Draft Assessment Paper, the functions of the Commonwealth government are quite different from those performed by State and Territory governments, so there is no reason to assume that relative needs of States and Territories would align across these two categories of expenditure.

Past Expense Assessments

Commission staff have suggested that past expense assessments could be used as a proxy for future expense assessments, given the stability of States' and Territories' assessed expenses over a 15 year period. Their analysis shows a growing divergence over time of States' and Territories' assessed expenses, as currently measured, from a set of "frozen" assessments. This divergence results both from changes in States' and Territories' circumstances and from changes in the Commission's measures of expense need over time.

This option would provide significant simplification benefits for Updates, but has some drawbacks. It would require periodic rebasing, presumably as part of a Review and some elements, such as infrastructure investment, may need to be separately assessed because of their volatility from year to year.

ACT Position

Subset of Existing Expense Assessments

The Draft Assessment Paper comments that the relationship between the subset of assessments and all the assessments is one of correlation not causation.

It is not clear why this should be considered a problem, as Commission assessments generally are built on correlation, with no attempt or need to identify causality.

However, it is questionable whether this option offers much in terms of simplification. Much of the present data collection and analysis would still have to be done. Changes in the underlying circumstances of States and Territories and in relative expenditure levels across assessments would require periodic review of the in-scope assessments and of their associated weights.

The variant of extrapolating from the largest expense assessments produces clearly inequitable outcomes, as shown by Table 9 of the paper (p.15). This is because of the exclusion of some 10 expenditure assessments in which the relative assessed needs of States and Territories obviously differ greatly from those in the four largest assessments.

Subset of State and Territory Attributes

The use of the subset of State and Territory attributes suggested by Commission staff would also create clearly inequitable outcomes, as shown by Table 11 (p.16). This is likely to be due to the selected attributes being inadequately representative of the factors affecting State and Territory expense needs across all assessments. Increasing the number of attributes would sacrifice any gains which could be made from simplification.

Regressions of State and Territory Actual Spending

The ACT agrees with the Commission staff conclusion that this approach is unlikely to prove useful given the limitations of the available data.

National Government Expenses

This approach would generate very large changes in GST distribution compared with the existing approach. Table 12 (p.19) shows a major redistribution from current recipient States and Territories to current donor States, moving the distribution substantially towards EPC. This is clearly not an equitable outcome and is inconsistent with the Commission's primary objective of HFE.

Past Expense Assessments

This approach represents a "freezing" of expense assessments, with a periodic rebasing process. It would adversely affect the contemporaneity of assessments, with low responsiveness to recent changes in State and Territory circumstances. It also involves a large redistribution of GST compared with the current approach, QLD, SA and TAS in particular being big losers.

Global Approach

The application of very broad macroeconomic measures (referred to as "global" measures by the Commission) to expenses, which is the logical corollary of the global approach to revenue, would suggest that a simple inverse approach might be applied in comparison with the revenue assessments.

That is to say, an above average GSP per capita would indicate lower expense needs per capita, given that an older, less healthy, more disadvantaged population would have a lower productive capacity per capita than a younger, healthier and more advantaged population. However, this option has not been canvassed by the Commission, possibly because such global measures are an even poorer indicator of States' and Territories' expenditure needs than they are of their revenue capacity.

The ACT's position on the use of global indicators of revenue capacity is set out above. Similar arguments apply to the use of global indicators to measure expense needs.

There are very significant differences in capacity in relation to States' and Territories' expenditure responsibilities, where some States and Territories carry a much heavier burden than others, on a per capita basis, due principally to the factors of indigeneity and remoteness, which are major drivers of cost differences between States and Territories. This is particularly the case for the NT, which has a much higher indigenous population share than the States and the ACT and a much higher proportion of its population living in remote and regional areas. The NT is an example in relation to expense needs which is analogous to that of differing distributions of revenue bases (e.g. property values) across States and Territories, where total values per capita may not reflect a significant difference in capacity. The NT has a high level of GSP per capita compared to the national average, but the distribution of its population by disadvantage and remoteness give it markedly higher expense needs than the national average.

The current redistribution of revenue from the Commonwealth to the States and Territories and between the States and Territories, to address VFI and HFI respectively, is intended to allow for differences in both revenue capacity and expense needs across these two sets of fiscal boundaries. As for revenue assessment, the use of global indicators for expense assessment could be made workable only through a fundamental reform of taxation powers and expenditure responsibilities to align States' and Territories' fiscal capacity with their broader economic capacity.

Commission's Current Approach to Simplification

Context

Since the 2010 Review, the Commission's primary tool for reducing complexity has been its disability materiality threshold. Only those disabilities that move more than the threshold are included. This technique is seen as an objective way of identifying and removing small disabilities.

Commission Staff Position

Commission staff have canvassed options for increasing the disability materiality threshold to \$100 per capita and \$200 per capita. These options would have a large negative impact on the smaller States and Territories, moving the GST distribution closer to EPC.

ACT Position

The ACT has consistently opposed the Commission's approach to reducing complexity through the use of materiality thresholds as arbitrary, detracting from equalisation and in practice not making the process simpler.

There is a substantial risk that materiality thresholds will not operate in a random manner across States, thus detracting from the equalisation objective, a risk which increases in its impact when thresholds are increased in proportion to total expenditure or revenue in a category. Increasing thresholds also gives the impression of simplification, but does not significantly reduce the assessment workload, as data gathering, analysis and calculation processes must still be carried out in order to determine whether an assessment generates a material difference in distribution or not.

Another key problem is the use of a threshold which is an absolute number, rather than a proportion. The effect of this methodology is that the more disaggregated a revenue or expenditure assessment is, the more likely it is that its components become immaterial. This applies even though, in aggregate, the components may have a material effect. Translating this issue across assessments means that those containing smaller dollar amounts are more likely to have immaterial redistribution effects and end up as EPC assessments, whereas in aggregate they may have a material effect. The current approach by the Commission takes no account of how such decisions to discount assessment components on materiality grounds might differentially affect States and Territories, i.e. some may be distinctly disadvantaged by it and others substantially advantaged.

The ACT proposes an alternative approach to materiality thresholds which would use a proportion (e.g. five per cent, 10 per cent) of the dollar amount in an assessment, or component of an assessment, which is redistributed as the minimum threshold for applying a differential assessment.

This would eliminate the effective requirement of the current approach which raises the level of the threshold as the dollar size of the assessment or component decreases. Commission staff should consider this proposal and assess the impacts of a few options for proportional thresholds.

We are strongly opposed to a large increase in the current materiality thresholds as being fundamentally inequitable. The Commission staff analysis as shown in Table 14 of the assessment paper clearly indicates that there is a fundamental conceptual problem with materiality thresholds, given that under one of the levels (\$200) four States and Territories would lose between \$175 and \$299 per capita, while the NT would lose \$580 per capita.

As pointed out in the Draft Assessment Paper, there is an underlying trade-off between simplicity and capturing States' and Territories' fiscal capacities. The simplification options presented by the Commission in their Draft Assessment Paper almost all have the effect of reducing the GST redistribution and impacting adversely on the smaller States and Territories. They all involve sacrificing the Commission's primary objective of equalisation for the secondary objective of simplification. Only options with minimal simplification gains do not have a major adverse impact on equity. Therefore, the ACT does not support any of the options for simplification presented in this paper.

PART C

SPECIAL CIRCUMSTANCES AND CHARACTERISTICS OF THE AUSTRALIAN CAPITAL TERRITORY

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SPECIAL CIRCUMSTANCES OF THE AUSTRALIAN CAPITAL TERRITORY

Summary

The ACT's special circumstances relative to other jurisdictions have not seen fundamental change since the last two major reviews of the application of the principle of HFE in the Commission's *Reports on GST Revenue Sharing Relativities – 2004 and 2010 Reviews*. The inherent difficulties and offsetting benefits arising from these characteristics are integral to the ACT Government's arguments and claims that permeate this 2020 Review submission. Principally, these circumstances arise from the ACT's different industry, demographic; employment, earnings; and household expenditure profiles relative to the other States.

Taking all of these factors together, it is apparent that the ACT's GST distribution is the result of circumstances beyond its control. It reflects the challenges faced by the ACT Government, relative to other jurisdictions, in raising revenue and providing services within a set of legal and geographic constraints imposed on it from outside.

The ACT's sustainability is highly dependent on the Commonwealth Government upholding a degree of responsibility for these special circumstances, as the risks posed to the ACT economy by it not doing so remain outside the ACT Government's control. This position arises both from the legal conditions of the ACT's self-government framework and from provisions in the Australian Constitution. These conditions remain in place today and will remain into the future.

Time has not ameliorated the fiscal impact of the special circumstances of the ACT on the ACT Government. The ACT Government does not agree with the presumption that after 29 years, it could be expected to have matured sufficiently to be able to deal with its historical legacies. This presumption does not recognise that these legacies are fundamental to the legal and institutional design of the ACT and are different to those faced by the States and the NT. Consequently, they continue to exert a major influence on the economic and fiscal management of the national capital.

While these characteristics impact on the ACT's GST share, they in themselves do not hinder the ACT Government's task of governing, as illustrated by the booming ACT economy. The conundrum for the ACT Government both now and in the future is that the HFE assessments illustrate that the ACT has a smaller base on which to raise revenue, but the ACT Government continues to deliver higher than average service provision.

INTRODUCTION

The Australian system of HFE has served the ACT well as it transitioned from a Commonwealth administered Territory to one with a limited form of self-government within the context of the wider Commonwealth. The system, while complex, is sound, complete, feasible and reasonably transparent; a system that is a global benchmark for other HFE models.

All States and Territories have vastly different circumstances that demand a centralised redistribution system, as represented by the HFE model in operation today, to ensure consistency in service delivery by all State and Territory governments across the nation. In the context of the ACT, the special characteristics of Canberra's roles as the national capital, seat of the Commonwealth Government, home of the APS and as a major regional centre continue to have economic and financial consequences for the ACT Government.

These consequences translate into an underlying financial and governance framework markedly different to the other States and Territories, requiring a high degree of cooperation between all responsible parties to ensure the ACT's sustainability. The ACT Government contends in this submission that HFE and the Commission's role in it has been critical to the development of this framework and will remain as important, if not more so, in the future. The special characteristics of the ACT are integral to the ACT Government's arguments and claims in this submission. Hence, it is considered timely to update the Commission of these characteristics and developments regarding them since they were last subject to a comprehensive workplace review in June 2008.

FOUNDATIONS OF THE AUSTRALIAN CAPITAL TERRITORY

The ACT was established on the traditional land of the Ngannawal people on 1 January 1911, as a compromise between NSW and VIC. Unable to accept the political and economic power of the national capital being concentrated in either State's capital city, NSW and VIC agreed to decentralise the national capital from its temporary home in metropolitan Melbourne to create an independent national capital. Canberra's establishment and continued existence thus constitutes an act of regional decentralisation from major metropolitan coastal cities for no other purpose than to serve as the national capital. Canberra is arguably the single greatest example of a successful decentralisation model, unparalleled anywhere in the world.

When the early governments of the Commonwealth decided to build a new city as the national capital, it was in recognition that it would be best to attract quality from all around the country to create a melting pot of ideas and innovation to assist government administration and good public policy. The process of the creation of the national capital was initiated by an international competition for the design of Australia's new capital city. The results were a simple but splendid concept from Walter Burley Griffin that forms the basis of the design of contemporary Canberra; the "Bush Capital".

It is through strength of commitment to Canberra as the home of the Commonwealth Parliament and APS that Canberra was successful. The functionality of the nation's capital today and into the future continues to rely on the Commonwealth Government working closely with the ACT Government. The ongoing deliberations of the Commission through the application of the principle of HFE is, while important, but one component of ensuring the financial wellbeing of the ACT.

CHARACTERISTICS OF THE AUSTRALIAN CAPITAL TERRITORY

The maintenance of the ACT's financial and governance framework was passed to the ACT Government on 11 May 1989, requiring it to administer the ACT on behalf of the Commonwealth Government. This framework, while ensuring the ACT remains a sustainable and independent member of the Commonwealth, results in the ACT having many different characteristics to the States and the NT, namely:

- A role as the national capital, seat of the Commonwealth Government and Parliament and home of the APS;

- The influence of the ACT's role as the national capital permeates all aspects of the ACT's economy, the lives of its citizens and the ACT Government's activities, from planning and development to the attributes of its workforce, population and industries. These traits require consideration in the 2020 Review across all assessments.
- A markedly different economy, reliant on the public sector and lacking in substantial manufacturing, primary industry and resource industries;
 - A highly concentrated economy and mobile workforce, which limit both the range of taxes which can be applied and the rates at which they are set; a key factor in the ACT's above EPC share of GST revenue.
- A city-state legislature, combining responsibility for State/Territory and local government functions with no counterpart in the Commonwealth;
 - A city-state model is an efficient system for the ACT due to its geographical size, while creating difficulties when comparing revenue raising and cost of service provision relative to other jurisdictions.
 - Conversely, the integrated system with access to the municipal tax regime, namely general rates, has facilitated the ACT's Government's tax reform strategy (discussed elsewhere).
- Commonwealth Government controls limiting the geographical size of the ACT and Canberra, including Commonwealth Government ownership of all land and joint planning responsibilities between the Commonwealth and ACT Governments;
 - The Commonwealth Government has maintained varying but strong levels of control over the development of the ACT, including the identification of the location of Canberra, Walter Burley Griffin's plans, Charles Weston's afforestation, John Sulman's garden city plans, William Holford's British New Town designs and the administration of the ACT by the National Capital Development Commission and the NCA. Self-government since 1989 has not, will not and cannot remove or reduce these influences to a level where it could be suggested the ACT Government has policy control over the ACT's development commensurate with the States and the NT.
- A different demographic profile to most other jurisdictions with consequential implications for service delivery and revenue raising opportunities;
- A markedly different geography and political boundaries; and
 - The ACT is a land-locked island within NSW and is the only jurisdiction with 100 per cent of the population living within 25 kilometres of another jurisdiction, thus creating cross-border considerations at an unmatched level.
- A role as the primary regional centre of Southern NSW.
 - Changes to the governance, economy and population of Canberra have a growing regional impact. The economy of the Canberra Region is significantly reliant on Canberra's role as the national capital and home of the APS.

Each of these circumstances manifests itself to varying degrees throughout the 26 revenue and expenditure assessments subject to this submission, whether it be in the form of a direct claim for national capital or cross-border allowance, by lower health expenditure needs due to a young population or by a lack of revenue capacity due to the inability to tax the Commonwealth Government. These overarching major characteristics are discussed further below and highlight, where relevant, significant structural change since 2010. Others are detailed elsewhere in the submission in response to specific assessments including industry, tax revenue sources and national capital and cross-border allowances.

Industry Characteristics of the Australian Capital Territory

The ACT economy is markedly different to all other jurisdictions in that it is dominated by the public sector. It has a highly specific economic profile due to the nature of its services and industries, the high proportion of people employed by the Commonwealth Government and in the relative size of the tertiary education sector, incorporating the Australian National University, the University of Canberra, the Australian Defence Force Academy, the Australian Institute of Sport and campuses of Charles Sturt University and the Australian Catholic University.

Over the year to the March quarter 2018, the Commonwealth Government represented 40.8 per cent of SFD in the ACT economy, down from its peak of 44.6 per cent in the year to the December quarter 2011, with expenditure in the ACT at approximately \$19.3 billion over the year to the March quarter 2018. The economic impact of the APS on the ACT economy is significant. The APS employs nearly 57,000 public servants in Canberra, representing 37.9 per cent of the total APS workforce, with the estimated wages spent in Canberra on the APS alone totalling over \$7 billion each year. Through the continued significance of the public service, these conditions have paved the way for the development of a knowledge-based service economy.

While the Territory has limited employment in manufacturing, agricultural and mining industries, it has seen strong growth in higher education, healthcare, professional services, ICT, defence, tourism and hospitality. In the period from 1995-96 to 2016-17, the gross value added by the manufacturing industry in the ACT grew by 5.8 per cent and primary industries¹ declined by 22.4 per cent, collectively. Nationally these industries grew by 9.1 per cent and 116.4 per cent respectively over this period.

Over the same period, industry gross value added by professional, scientific and technical services grew in the ACT by 340 per cent, healthcare and social assistance by 230.2 per cent and administrative and support services by 111.2 per cent, compared with 167.3 per cent, 151.8 per cent and 97.5 per cent nationally. The share of these three industries increased from 13.6 per cent of GSP in the ACT in 1995-96 to 23.4 per cent in 2016-17, while public administration and safety's share of GSP increased from 24.9 per cent to 26.7 per cent (Table C.1).

¹ These are the *agriculture, forestry and fishing* and *mining* industries.

Table C.1: Share of GSP by Industry, ACT and Australia

	Australia		ACT	
	Per cent		Per cent	
	1995-96	2016-17	1995-96	2016-17
Agriculture, forestry and fishing	2.99	2.77	0.15	0.05
Mining	4.68	5.92	0.11	0.05
Manufacturing	10.31	5.84	1.67	0.88
Electricity, gas, water and waste services	3.61	2.44	3.76	1.90
Construction	5.89	7.38	4.14	5.74
Wholesale trade	4.02	4.20	1.25	1.03
Retail trade	3.95	4.47	2.76	3.29
Accommodation and food services	2.60	2.41	3.25	1.82
Transport, postal and warehousing	4.84	4.81	2.43	1.97
Information media and telecommunications	2.09	2.66	2.93	3.52
Financial and insurance services	6.55	8.79	3.57	3.08
Rental, hiring and real estate services	2.99	3.06	2.09	2.27
Professional, scientific and technical services	4.89	6.78	4.56	10.01
Administrative and support services	3.08	3.16	2.43	2.56
Public administration and safety	6.23	5.49	24.85	26.68
Education and training	5.88	4.87	8.20	5.60
Healthcare and social assistance	5.41	7.07	6.57	10.81
Arts and recreation services	0.76	0.82	0.53	0.69
Other services	2.19	1.67	2.86	1.71

Sources: ABS cat. No. 5220.0 and 5206.0

The transformation in the ACT economy has been most visible in the ACT's service export performance.

Over the five years from 2011-12 to 2016-17, the ACT's average annual services export growth has been 7.3 per cent. While the ACT's population share is 1.7 per cent of the national population, its share of national services exports was 2.4 per cent in 2016-17.

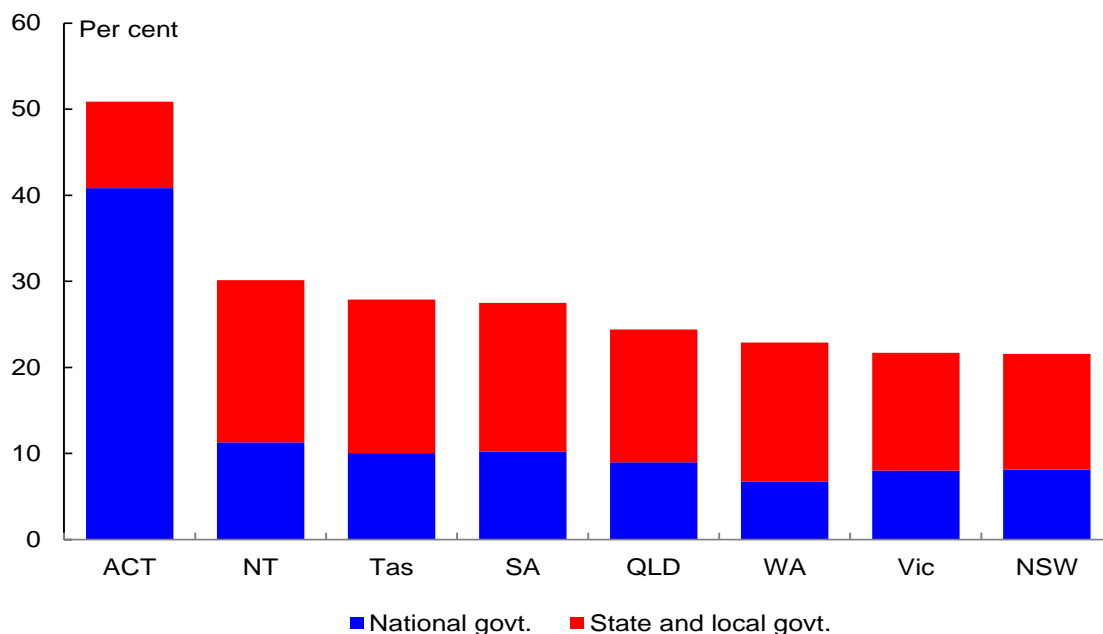
This comparison of the ACT economy with the national economy highlights the ACT's continued dependence on the public sector and related services. It also means that while the ACT economy has diversified, it is still heavily influenced by Commonwealth Government decisions relating to the ongoing size of the APS.

The proportionate size of the APS in the ACT is almost entirely outside the control of the ACT Government. As such, structural changes in and diversification of the ACT economy have occurred primarily in the non-Commonwealth Government sectors, as opposed to the relative size of the Commonwealth Government to the rest of the ACT economy. Diversification of the ACT economy has aided in the ACT economy growing by 4.6 per cent in 2016-17; the highest rate of any State or Territory, despite little contribution from the public sector to this growth. This in turn has resulted in the ACT economy becoming more resilient to changes in Commonwealth Government policy, including job losses in the APS.

However, the Commonwealth Government remains the dominant economic force in the ACT. In no other jurisdiction does Commonwealth Government policy have such a significant impact on the economy. A Commonwealth Government decision to cut APS staff or public investment in the ACT can have significant flow on effects for the ACT Government. Figure C.1 describes the importance of Commonwealth, State and Territory and local government expenditures, as a share of SFD in the ACT and in comparison to other jurisdictions.

Figure C.1: Government expenditures as a share of SFD

Source: ABS cat. no. 5206.0.



Note that public corporations' expenditures are included in government expenditures.

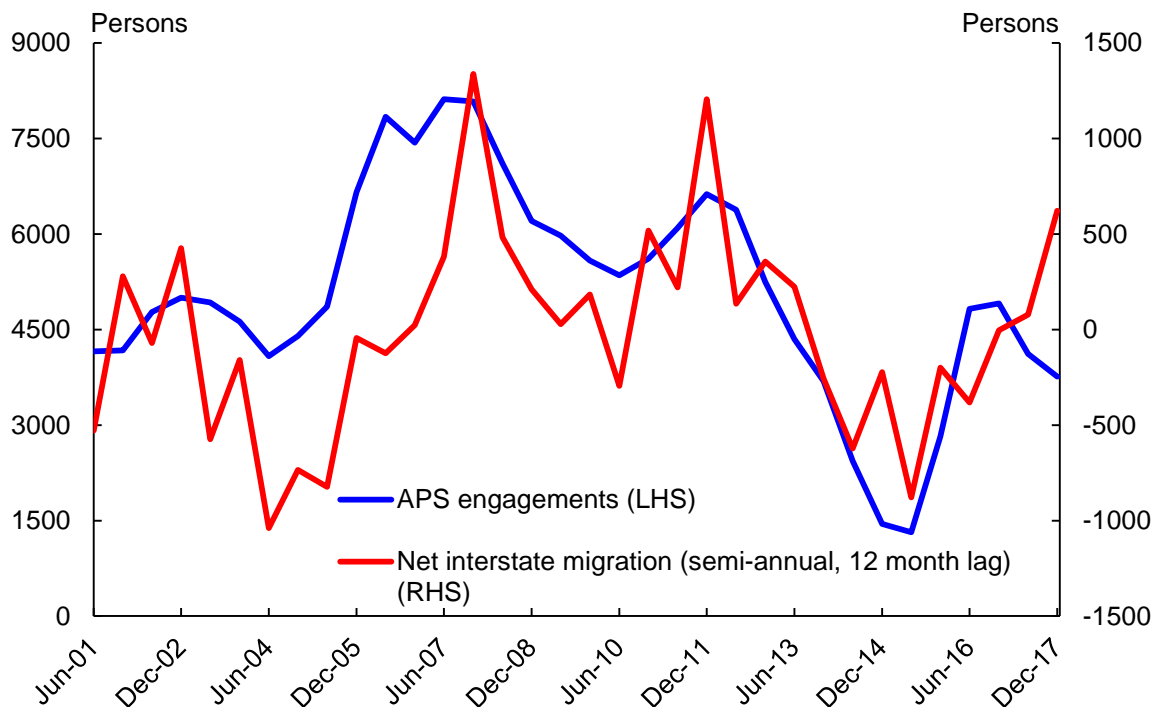
Demographic Characteristics of the Australian Capital Territory

In June 2017, the proportion of young adults between 20 and 34 years of age was relatively high in the ACT (25 per cent) compared with Australia as a whole (22 per cent). This section of the population tends to be highly mobile relative to older cohorts, increasing the significance of internal migration between the ACT and the States and NT.

The prevalence of high quality educational institutions within the ACT attracts young people to the ACT to study. The nature of the workforce also presents opportunities for better educated individuals.

However, the labour market in the ACT is highly dependent on Commonwealth Government policy and changes in the size of the APS strongly influence work prospects. Figure C.2 illustrates how changes in APS hiring impacts on labour mobility in the ACT, plotting the number of APS engagements against Net Interstate Migration.

Figure C.2: APS engagements (hirings) and Net Interstate Migration (one year lag), ACT, 2001 to 2017.



Sources: ABS cat. no. 3101.0 and APS Employment Database.

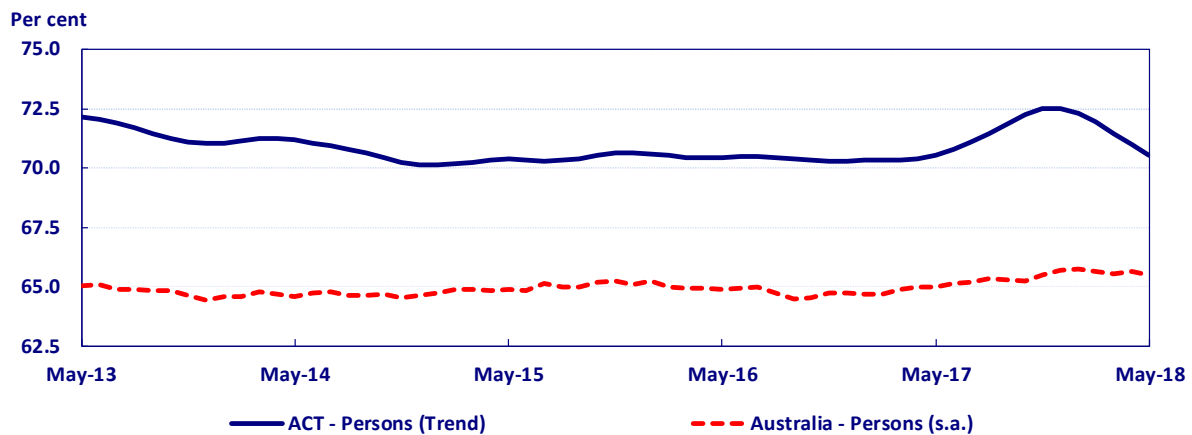
This creates difficulty for the ACT Government in planning land releases and economic development, service provision and revenue raising. It can also limit the revenue base available to the ACT and the ways in which that base is taxed.

The ACT is home to a number of disadvantaged people and households of low SES. Analysis done on a geographical basis can mask this because of the diversity of socio-economic composition of the areas within the ACT. The ACT has a high level of socio-economic diversity within its statistical areas. For example, in 2016-17, the ACT had the highest GHD per capita of all States and Territories. At the same time, in 2016-17 the number of clients per 10,000 population accessing homelessness services in the ACT was the fifth highest of any jurisdiction.

Employment and Earnings Profile of the Australian Capital Territory

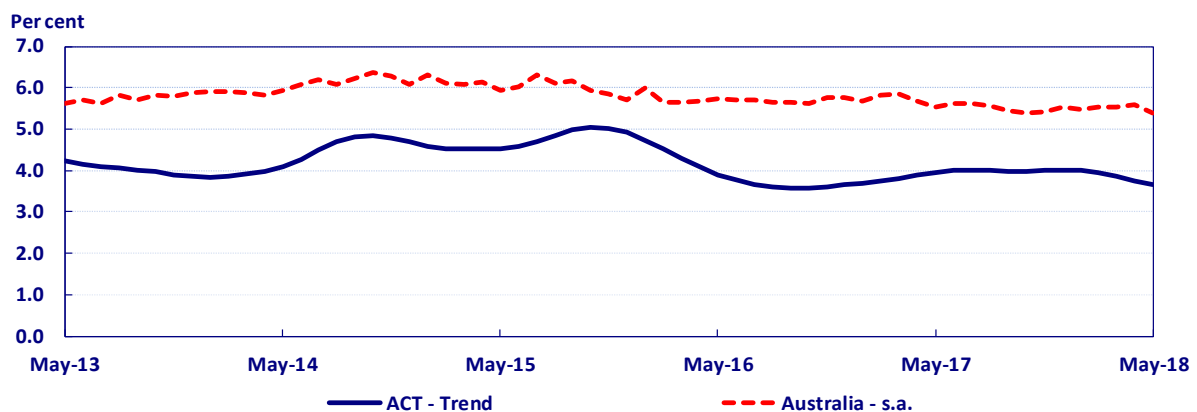
As at April 2018, the ACT participation rate was 70.5 per cent, well above the national rate of 65.5 per cent. At the same time, the ACT's unemployment rate of 3.7 per cent is well below the national rate of 5.4 per cent and the lowest of any jurisdiction. These measures are consistently better than the national rates (see Figure C.3 and Figure C.4).

Figure C.3: Participation rate, ACT and Australia



Source: ABS cat. no. 6202.0, April 2018

Figure C.4: Unemployment rate, ACT and Australia



Source: ABS cat. no. 6202.0, April 2018

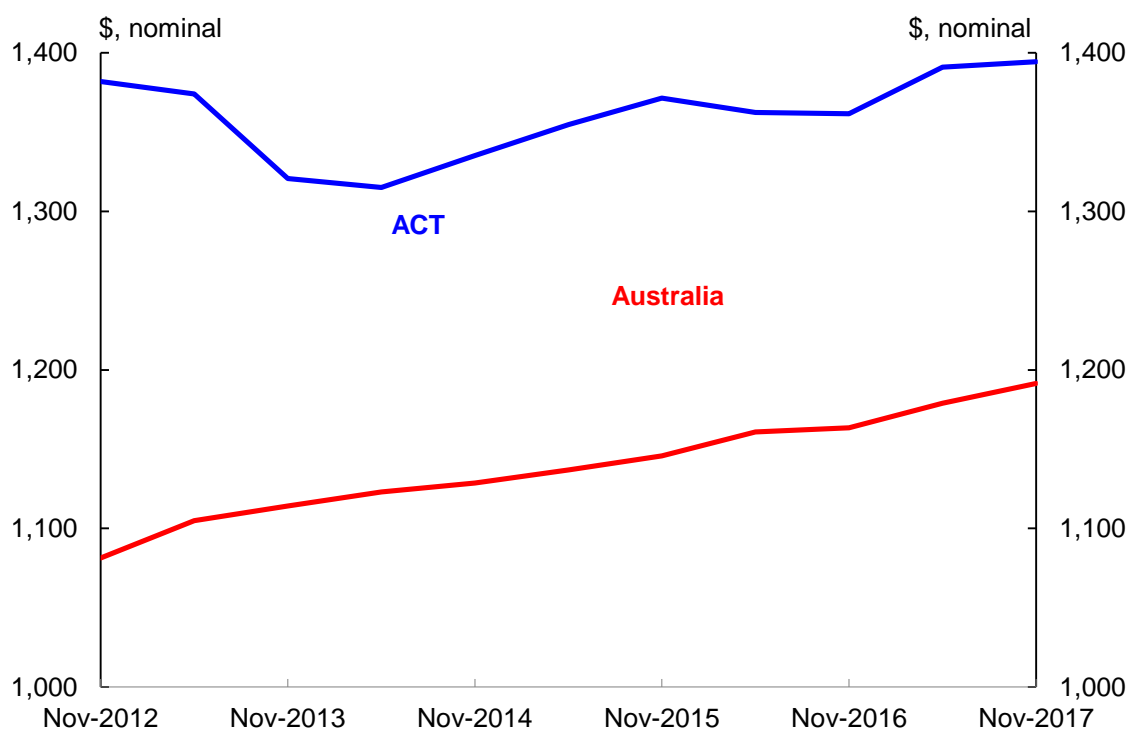
Workforce participation in the ACT is further characterised by full time employment accounting for 74 per cent of total employment, compared with 68 per cent nationally.

Given the proliferation of tertiary education institutions in the ACT and the above average proportion of young adults, it could be expected that part time work would play a more significant role in the job market overall.

As at February 2018, almost 60 per cent of ACT employment was within the categories of professional, scientific and technical services, public administration and safety, education and training and healthcare and social assistance. By comparison, these categories made up 35.7 per cent of employment nationally. Employment within these classifications in most cases requires tertiary education qualifications.

The State of the Regions report, prepared by National Economics on behalf of ALGA, named the ACT the disposable income capital of Australia. Average Weekly Earnings for the ACT are generally significantly higher than Australia overall and are the highest of any State or Territory (see Figure C.5).

Figure C.5: Average Weekly Earnings (Fulltime Ordinary time earnings), ACT and Australia



Source: ABS. Cat. no. 6302.0, November 2017

Between November 2012 and November 2017, Average Weekly Earnings increased by 0.9 per cent in the ACT while nationally it increased 10.2 per cent. The substantial difference in performance over this time is due to the effect of the Commonwealth public service hiring freeze and the subsequent effect on the ACT economy. The gap between average weekly earnings in the ACT and nationally narrowed by one third over this time, to around \$200 per week.

Moreover, while the ACT has seen significant growth in the services industries, a number of these sectors are still heavily influenced by the public sector. Consequently, the ACT's Average Weekly Earnings continues to be impacted by fluctuations in Commonwealth Government expenditure and movements in APS employment.

Household Expenditure Characteristics of the Australian Capital Territory

The 2015-16 ABS Household Expenditure Survey found that households in the ACT recorded one of the highest average weekly expenditures of all States and Territories, second only to the NT. Canberra residents also had significantly higher weekly expenditure than the average in other capital cities.

In 2015-16, average weekly household expenditure in Canberra was \$1,670 per week. This was \$134, or 8.7 per cent greater than the average expenditure of all Australian capital city households.

Summary of Economic Characteristics of the Australian Capital Territory

When considering all of the ACT's economic characteristics, it makes for a rather contrasting picture.

On the one hand, the ACT displays characteristics that would suggest a strong capacity to raise its own revenue; highly educated, well paid employees working in a job market with high levels of participation and low levels of unemployment.

The ACT's knowledgeable populace lends itself to leading the nation in service delivery and reform. The ACT Government has unilaterally undertaken an extensive tax reform strategy that gradually phases out some of the most inefficient taxes and replaces that revenue with better designed taxes on more efficient tax bases. The ACT was also the first jurisdiction to deregulate its taxi industry and legalise ride sharing.

The standard of living in the ACT would certainly support this view. The State of the Regions report prepared for ALGA claimed the ACT was the disposable income capital of Australia and international analysis has also illustrated the ACT's strengths. The Organisation for Economic Cooperation and Development ranked the ACT first amongst Australian jurisdictions in terms of jobs and income in its 2016 Regional Wellbeing Report. Across all 11 wellbeing categories, the ACT ranked first in six and second in four.

However, the ACT Government faces a range of challenges. The highly educated population is also young and highly mobile. Combined with a geography where all residents reside within 25 km of another jurisdiction, this does not allow for a great deal of flexibility in the way its revenue bases are taxed.

The higher educated constituency, a number of whom are engaged in public policy in one form or another on a daily basis, also demand higher service provision. The need to fund higher quality education, healthcare and housing places considerable strain on governments to fund these services adequately.

Performance of the Australian Capital Territory Economy

Recent Economic Performance

While these characteristics impact on the ACT's GST share, they in themselves do not hinder the ACT Government's task of governing.

The ACT economy is strong and growing, recording the fastest economic growth of any State or Territory in 2016-17 (4.6 per cent). A recent Deloitte Access Report stated that Canberra is a major hub for information technology, cyber security, defence, intelligence and other high skilled professional jobs.

As indicated earlier, the ACT is also a growing hub for the university education of international students. Education is the ACT's biggest export and grew by 24 per cent in 2016-17, with the sector now contributing in excess of \$780 million to the ACT economy each year. The ACT International Education Strategy, launched in September 2016, sets out a plan to increase the education sector's contribution to Canberra's economy, including employment outcomes through a collaborative approach with all education providers. It sets a number of goals including consistent, sustainable growth in enrolments and associated jobs, export and investment outcomes.

Jobs in other industries are also continuing to expand. The ACT's construction industry in particular is experiencing significant growth, with housing, commercial and public infrastructure spending all continuing at a rapid pace.

Jobs in retail trade, information media and telecommunications, administrative and support services and healthcare and social assistance are also growing in the ACT. The latest ABS employment data shows that the ACT has the lowest rate of casualisation of the workforce of any State or Territory in Australia.

The ACT Government has long identified the risk posed to the economy by Commonwealth job reductions and, in recent times, decentralisation of the APS. In order to mitigate these risks, the ACT Government has made it a priority to diversify the economy.

While the ACT Government has almost no control over Commonwealth Government policy and thus APS hiring, the ACT Government has sought to improve the resiliency of the ACT economy through building other major industries. Such industries, as alluded to above, include professional, scientific and technical services and healthcare and social support, which now consist of a combined 20.8 per cent of the ACT's GSP. This compares to 26.7 per cent for public administration and safety. Growth in these key sectors has also helped to drive the ACT's recent strong economic performance.

Economic Outlook

The ACT, like all other jurisdictions, faces mounting fiscal pressures. The factors driving this in the ACT are population growth and wage and input costs growth.

The ACT is prosperous. Furthermore, the amenity of Canberra is high, with economic infrastructure that supports the efficient movement of people and goods and social infrastructure that allows for the delivery of high quality public services.

Much of this prosperity, however, has been built on the foundation laid by the Commonwealth Government, which provided the ACT community with significant resources in terms of land and high quality economic, social and cultural infrastructure. The location of the APS in the ACT has underpinned growth in high skilled jobs for decades and it is these jobs which, in turn, support local economic activity and ultimately the revenue bases which fund ACT Government services.

However, the ACT has reached a point where reliance on the Commonwealth Government as the key driver of prosperity can no longer be assured. Recent Commonwealth Governments have not shown a desire to make large scale city building investments like their predecessors and the ACT's rapid population growth has begun to outgrow the creation of new jobs in the APS. In 2012, 30.2 per cent of total ACT employees were in the APS, in 2017 it had fallen to 24.3 per cent². Automation of jobs combined with tight fiscal policy indicate static or decreasing Commonwealth Government job creation over the long term.

The ACT also continues to deplete its land resources to satisfy demand for housing (low cost development fronts are expected to be exhausted by 2040) and infrastructure inherited from the Commonwealth Government is either approaching full capacity, the end of its useful life (such as a number of schools and community facilities) or both (such as the Canberra Hospital). The ACT Government estimates that the ACT's population will pass 500,000 in 2032. These estimates predict that the number of Canberrans will increase by over 100,000 from the end of 2017 to the end of 2032, a 25.8 per cent increase in 15 years.

² Refer to the number of APS for the month of December.

The size of this increase in population is expected to require the construction of more than 30,000 dwellings and will increase demand on ACT Government service provision and the need for public infrastructure. Additionally, healthcare and education costs in particular are projected to grow at rates well above the projected growth rates of State and Territory tax revenues. Health expenditure is expected to grow at an average annual rate of 6.0 per cent and education expenditure at 5.1 per cent.

Managing this anticipated growth will require future governments to apply many public policy levers, not just those involving tax policy settings. Improving the effectiveness of government spending to free up resources to reinvest in more effective initiatives is paramount. The objective of a well-ordered city with high amenity is also critical in attracting business investment and talent, which are the key ingredients of future economic prosperity.

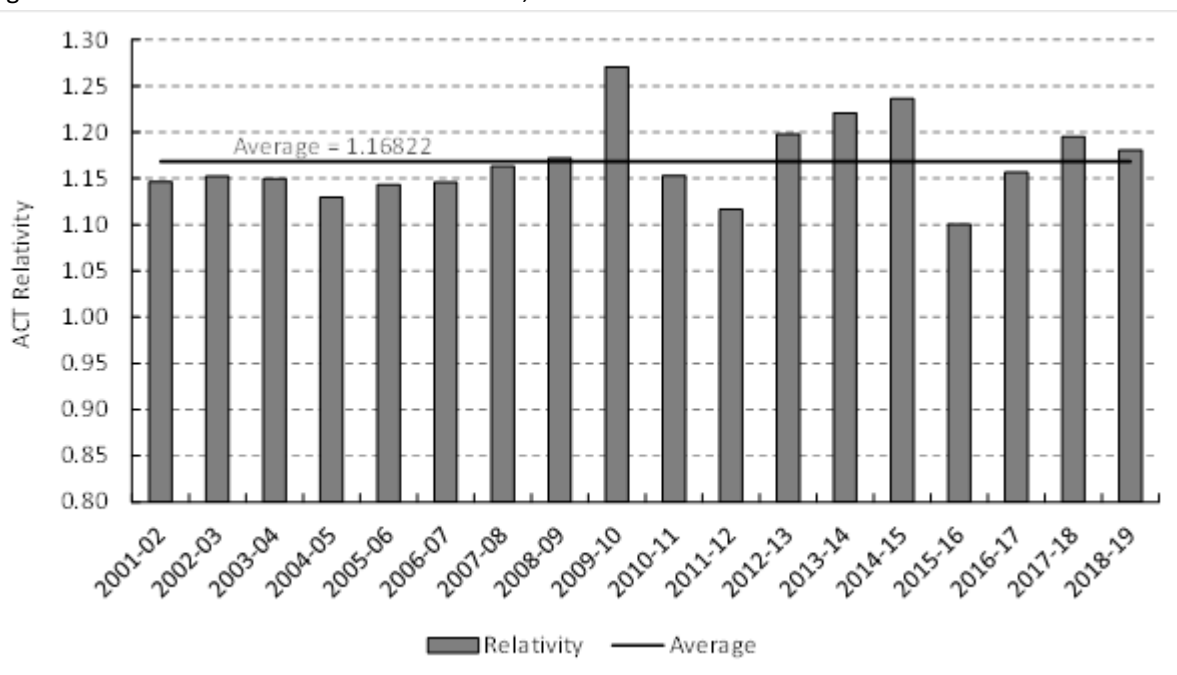
To address these issues in future, the ACT will face difficult questions about the types of services made available and the level of taxation effort required. The ACT generally provides higher than average levels of government services. The maintenance of those service levels will place greater pressure on the revenue base. This will require careful consideration on the part of the ACT Government both now and in the future.

IMPACT OF THE SPECIAL CHARACTERISTICS OF THE AUSTRALIAN CAPITAL TERRITORY ON HORIZONTAL FISCAL EQUALISATION

These special characteristics explain why the ACT is the second least dependent on Commonwealth Government revenue of any State or Territory, while also receiving an above population share of GST. The key element is that the GST methodology does not look at the circumstances of the States and Territories in isolation, but rather compares them with each other. In isolation, the ACT's capacity to raise its own revenue appears high. High household incomes and high engagement in the workforce make the ACT labour force appear like a strong tax base. Broad measures of economic capacity such as GSP per capita also support that perception.

However, these characteristics become much less significant when compared to other jurisdictions. The HFE methodology is based on national averages. The ACT, being a small economy, has minimal impact on these averages, with the distribution largely being driven by changes in the revenue capacity and expense needs of the larger States. Considering this, the special characteristics of the ACT, all of which are beyond its control, combine to create an assessed GST requirement that is consistently above an EPC share.

Figure C.6: Historical GST relativities of the ACT, 2001-02 to 2018-19.



Source: 2018-19 ACT Budget

The Commission had a key role in preparing for the introduction of self-government in the ACT. The move towards self-government was based on an understanding that the ACT’s fiscal needs would be taken into account in accordance with the principle of HFE. Before the ACT’s representatives agreed to the terms for self-government, obtained assurances from the Commonwealth Government that it would provide for the Commission to make recommendations about their needs for general revenue grants.

The ACT became a self-governing Territory on 11 May 1989 under the *Australian Capital Territory (Self-Government) Act 1988*. Section 59(1) of the Act provided that:

...“the Commonwealth shall conduct its financial relations with the Territory so as to ensure that the Territory is treated on the same basis as the States and the Northern Territory, while having regard to the special circumstances arising from the existence of the national capital and seat of Government of the Commonwealth in the territory”.

This legal condition promoted the development of financial mechanisms specifically designed to ensure the sustainable existence of the ACT as a fully functioning member of the Commonwealth. These mechanisms provided the ACT a capacity to raise own source revenues and receive federal funding commensurate with the States and the NT while also receiving funding in recognition for the aforementioned special characteristics of the ACT. This in turn gave the ACT Government the capacity to provide services and the associated infrastructure at the same standard as the other jurisdictions.

After four separate Commission inquiries into ACT Government finances (two before self-government and two after) the 1992 Premiers Conference decided to base the ACT's general revenue assistance for 1992-93 on the per capita relativity assessed by the Commission. This undertaking remains in place today and looks to remain into the future.

Time has not ameliorated the fiscal impact of the special circumstances of the ACT on the ACT Government. The ACT Government considers the presumption that after 29 years, the ACT Government could be expected to have matured sufficiently to be able to deal with historical legacies, just as all other State and Territory Governments have been expected to address theirs, is conceptually flawed, because these legacies are fundamental to the legal and institutional design of the ACT. Consequently, they continue to exert a major influence on the economic and fiscal management of the national capital.

PART D

DRAFT ASSESSMENT PAPERS

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OVERVIEW OF THE DRAFT ASSESSMENT PAPERS

Summary

Commission staff released Draft Assessment Papers on all assessments to the States and Territories with an invitation to submit comments by 31 August 2018. This submission reflects a whole-of-government response to the Draft Assessment Papers co-ordinated by the Chief Minister, Treasury and Economic Development Directorate.

The ACT agrees with the adopted scope of State and Territory activities covered in the Draft Assessment Papers and notes that the scope is the same as that of the 2015 Review. The ACT also agrees with the proposed assessment structure for the 2020 Review, noting that it is also the same assessment structure as the 2015 Review with the one exception; a proposal to combine depreciation and investment into a single Physical and Financial Assets assessment. The ACT considers that this approach is logical and ensures a high degree of consistency between Reviews.

The ACT also supports the staff proposal to retain most disabilities assessed in the 2015 Review, noting that the changes proposed in the draft assessment papers appear to reflect incremental improvements to the measurements of disabilities, most of which are welcomed. The ACT does not agree with the Commission staff on some disabilities, particularly those for national capital planning and cross-border allowances. Similarly, in other instances the ACT also proposes changes to the extent and coverage of a number of the disabilities to specific assessments.

The ACT also acknowledges that as Commission staff progress the 2020 Review, there will be an ongoing requirement for additional consultation prior to the release of the draft 2020 Review Report in May 2019.

PROPOSED SCOPE OF ACTIVITIES AND ASSESSMENT STRUCTURE FOR THE 2020 REVIEW

The ACT agrees with the adopted scope of State and Territory activities covered in the Draft Assessment Papers and notes that the scope is the same as that of the 2015 Review. This ensures the range of activities includes all State and Territory general government sector activities and urban transport and public housing PNFCs, as defined by the updated Australian 2015 GFS framework. The ACT considers that this approach is logical and ensures a high degree of consistency between Reviews, a welcome approach and consistent with the stated objectives of the 2020 Review quality assurance strategy.

The ACT also agrees with the proposed assessment structure for the 2020 Review, noting that it is also the same assessment structure as the 2015 Review with the one exception; a proposal to combine depreciation and investment into a single Physical and Financial Assets assessment.

PROPOSED DISABILITY ASSESSMENTS FOR THE 2020 REVIEW

The ACT also supports the staff proposal to retain most disabilities assessed in the 2015 Review.

ACT GOVERNMENT RESPONSE ON COMMONWEALTH GRANTS COMMISSION 2020 REVIEW DRAFT ASSESSMENT PAPERS

In line with the proposed 2020 Review quality assurance strategy objective of ensuring consistency between Reviews, the changes proposed in the Draft Assessment Papers appear to reflect incremental improvements to the measurements of disabilities, most of which are welcomed, namely:

- Use of better data;
- Improvement in assessment methodology;
- Better targeting of disabilities;
- Adapting assessments to better capture changes in average policy; and
- Using broader indicators where appropriate.

Noting that for the expenditure assessments where Commission staff are not proposing to assess new disabilities, but are proposing to stop assessing some, particularly national capital planning and cross-border allowances, the ACT argues for the retention of some of these disabilities as outlined in the relevant chapters. Similarly, in other instances the ACT also proposes changes to the extent and coverage of a number of the disabilities relating to specific assessments.

Finally, the ACT acknowledges that as Commission staff progress the 2020 Review, there will be an ongoing requirement for additional consultation prior to the release of the draft 2020 Review Report in May 2019.

REVENUE ASSESSMENTS

PAYROLL TAX

Summary

The Payroll Tax assessment differentially assesses each State and Territory's ability to generate revenue from payroll taxes. Payroll taxes are levied on the employee expenses of firms operating within each State and Territory's borders which are higher than a general deduction threshold. The general deduction threshold varies between the States and Territories.

The ACT supports the proposal to retain the 2015 Review approach, but has concerns with the volatility of CoE data on the basis of frequent data revisions causing unpredictable variations in the ACT's assessed payroll tax capacity. The ACT proposes that the Commission explore alternatives to the CoE dataset to use as the basis for the Payroll Tax assessment.

The ACT also proposes an adjustment to improve the methodology by accounting for common exemptions and concessions between the States. This proposal would result in employee expenses paid by charities and non-profit organisations being excluded from each State and Territory's assessed tax base, reflecting the fact that most States do not levy payroll tax on such organisations. The ACT has calculated that the proposal would result in a material impact on the GST distribution, with approximately \$276 million, or \$11.49 per capita in additional redistribution occurring nationally and three States having more than \$30 per capita being redistributed towards or away from them. The ACT considers that this proposal would enhance the assessment's accuracy and conformity to the principles of *What States Do* and *Policy Neutrality*.

Context

As part of its assessments of State and Territory revenue raising capacity and expenditure needs, the Commission calculates the ability of States and Territories to raise revenue from payroll taxes. In accordance with the methodology set in the 2015 Review, the Commission currently assesses each State and Territory's capacity to generate revenue through payroll taxes on the basis of ABS national accounts data on CoE, supplemented with ABS data on wages and salaries to remove remuneration paid by the general government sector and employee expenses below the national average payroll tax threshold.

The Payroll Tax assessment redistributed \$1.575 billion, or \$63 per capita in the 2018 Update, including \$7 million, or \$17 per capita in additional GST to the ACT.

Commission Staff Position

2018-10-02-S proposes that the methodology for assessing State and Territory Payroll Tax revenue remain unchanged from the approach developed in the 2015 Review. This recommendation was made on the basis that the Commission did not identify any issues in the Payroll Tax assessment for the 2020 Review.

The Commission had considered possible methodology changes to better reflect progressive payroll tax systems through diminishing payroll tax thresholds, however it rejected this proposal on the basis of practicality concerns due to an unavailability of ABS data on wages and salaries by company payroll size.

The Commission also noted that it is not aware of any suitable alternative dataset to ABS CoE data for the assessment and that possible tax elasticity effects on the Payroll Tax assessment will be addressed by the ongoing tax elasticity consultancy at a later date.

ACT Position

The ACT supports the Commission’s position to retain the 2015 Review methodology for the Payroll Tax assessment, as well as its decision to not introduce an assessment of diminishing payroll tax thresholds.

The ACT does note however that CoE data over recent years has produced highly volatile Payroll Tax assessment outcomes for the ACT, due principally to frequent data revisions by the ABS. In the 2018 Update. The ACT was affected by an estimated \$44 million loss of GST funding due to revisions to ABS CoE data and a \$53 million, or \$126 per capita loss in GST revenue from the Payroll Tax assessment overall. This compares to a \$57 per capita increase in assessed GST need from the Payroll Tax assessment for WA; the jurisdiction with the next biggest change (Table D.1).

Table D.1: Changes in ACT assessed GST need from Payroll Tax assessment, 2015 Review to 2018 Update

Application Year	2015	2016	2017	2018
ACT change in assessed GST (\$ per capita)	-88	+90	+37	-126
Impact on ACT (\$ million)	-35	+36	+15	-53
(Next) highest change in assessed GST (\$ per capita)	-57 (WA)	-100 (NT)	+44 (WA)	+57 (WA)

Source: Commonwealth Grants Commission

During the period since the 2015 Review, the ACT’s assessed Payroll Tax revenue for the same assessment years has fluctuated over a range between \$66 and \$91 per capita. This range implies an impact between \$26m and \$36m in each year, a very significant amount for the ACT Budget. The ACT’s CoV for assessed Payroll Tax capacity is also much higher than that for the other States and the NT between 2012-13 and 2015-16, with most CoV’s for the other States and the NT being less than one per cent compared with around six percent for the ACT (Table D.2). This contrasts with a CoV for the ratio of the ACT’s WPI against the national WPI over the same period (June 2013 to June 2016) of 0.09 per cent and of the CoV for the ratio in the ACT’s number of employed people against the national number of employed people of 1.34 per cent (Table D.3). This indicates that the level of variation of the ACT’s assessed Payroll Tax capacity would be expected to be significantly lower than it has proven to be.

**ACT GOVERNMENT RESPONSE ON COMMONWEALTH GRANTS COMMISSION 2020
REVIEW DRAFT ASSESSMENT PAPERS**

Table D.2: ACT assessed Payroll Tax capacity across application years, 2011-12 to 2016-17

Application Year	2015	2016	2017	2018	Mean	ACT CoV	State/Territory Average CoV
ACT assessed Payroll Tax capacity (\$ million)							
2011-12 assessment year	985				985		
2012-13 assessment year	948	875			912	5.66	0.38
2013-14 assessment year	869	803	803		825	4.62	0.37
2014-15 assessment year		791	794	882	822	6.29	1.25
2015-16 assessment year			813	903	858	7.42	1.54
2016-17 assessment year				983	983		

Source: Commonwealth Grants Commission and ACT Treasury calculations

Note: State/Territory Average CoV excludes ACT

Table D.3: ACT WPI and employment relative to national WPI and employment, 2013 to 2016

Data release date	June 2013	June 2014	June 2015	June 2016	Mean	CoV
ACT WPI	113.4	116.1	118.8	121.2		
National WPI	114.4	117.3	120.1	122.5		
ACT to national WPI ratio	0.9913	0.9898	0.9892	0.9894	0.9899	0.09
ACT employed persons (‘000)	213.5	215.3	213.3	218.6		
National employed persons (‘000)	11,503.3	11,571.1	11,774.7	12,005.3		
ACT to national ratio of employed persons	0.0186	0.0186	0.0181	0.0182	0.0184	1.34

Source: ABS 6345.0, ABS 6202.0 and ACT Treasury calculations

The frequent revisions in CoE data and subsequent fluctuations in the ACT’s assessed Payroll Tax capacity is inconsistent with the Commission’s own criteria for quality data according to Draft Assessment Paper 2018-01/01-S (page five):

“We have used the 2020 Review assessment guidelines, as set out in Commission Position Paper CGC 2017-21, The principle of HFE and its implementation, to assist in the review of the assessments. The guidelines say that the Commission will include a disability in a category when... data are available that are of suitable quality – the collection process and sampling techniques are appropriate, the data are consistent across the States and over time and are not subject to large revisions”

Noting the volatility in the GST distribution due to data revisions in relation to payroll tax, options to improve the data accuracy should be considered. In light of the cost associated with increasing the size of ABS surveys, consideration of a new data set would be preferable to improving the accuracy of the CoE. ATO personal income data could be explored as an alternative to the CoE data for measuring the payroll tax base. ATO data could be sourced from the ABS who have access to this data or a separate request to the ATO could be made by the Commission.

The ACT further proposes that the Payroll Tax assessment methodology be refined to take common payroll tax exemptions across the States and Territories into consideration. States and Territories provide exemptions and concessions on payroll tax to a variety of different employer types and for certain types of employees, wherein employers are not required to pay payroll tax on a portion or all of their employee expenses if they meet certain conditions. The concessions and exemptions that are offered vary across the States and Territories, however, there are a number that are common across jurisdictions.

The ACT has identified payroll tax exemptions to non-profit organisations and charities as one such common concession, with VIC being the only jurisdiction that does not exempt non-profit organisations and charities from paying payroll tax. Consequently, States and Territories that have an above-average percentage of their workforce employed by large charities and non-profit organisations have a lower capacity to generate revenue from payroll tax compared with States and Territories that have a below-average percentage of their workforce employed by non-profit organisations and charities.

The Commission does not at present make an adjustment to account for common exemptions, such as those afforded to non-profit organisations and charities.

The ACT considers that, as the exemption of non-profit organisations and charities is common across States and Territories, the Commission acknowledging the consequent reduced revenue capacity from the exemption would be consistent with the *What States Do* and *Policy Neutrality* principles of HFE. The ACT considers on this basis that the common exemption of non-profit organisations and charities should be incorporated into the Payroll Tax assessment.

The ACT notes that the ABS does not provide data on CoE in the non-profit and charity sector. Rather, ABS CoE data is split by private and public employers. Thus, CoE data for non-profit organisations and charities is captured under the private sector split of the ABS CoE data, but there is no way to separate this data out from other private sector entities. Therefore, an alternative to ABS CoE data would be required to enable a differential assessment on the basis of non-profit and charity sector CoE.

To this end, the ACT has identified the Australian Charities Report, prepared on an annual basis since 2014 by the Centre for Social Impact and Social Policy Research Centre using data lodged by charity and non-profit organisations to the ACNC, as a potential data source for the assessment.

The Australian Charities Report consists of a comprehensive breakdown of the characteristics of different non-profit organisations and charities, including but not limited to the number of organisations, their size, location, revenue, expenses, sector and remoteness. Importantly, the Australian Charities Report also contains information on the amount of employee expenses incurred by non-profit organisations and charities of different sizes. As well as being published in the Australian Charities Report, the data is also available online via an interactive Tableau data cube.

The Australian Charities Report is compiled on the basis of Annual Information Statements that Australian charities and non-profit organisations are required to lodge with the ACNC. All charities and non-profit organisations must register with the ACNC in order to receive Commonwealth Government tax concessions. Further, financial information for medium or larger non-profit organisations and charities is required to be independently audited prior to being submitted to the ACNC as part of the Annual Information Statement. On the basis of these controls, the ACT considers that the data is reliable and the Australian Charities Report is the most comprehensive dataset that the ACT has been able to identify.

As a proof of concept for the adjustment, the ACT calculated Taxable Private Sector CoE for the 2015/16 financial year by taking the product of Private Sector CoE and the Private Sector Taxable Proportion as specified in ASOL for the 2018 Update. The 2015/16 financial year was used for the calculation as it is the most recent financial year reported in the Australian Charities Report (2016).

Employee expenditure data from the Australian Charities Report was used to determine the proportion of CoE paid by charities and non-profit organisations. As with Private Sector CoE, an adjustment to this data was required to account for employee expenses which fall below the payroll tax threshold. To allow for this, splits were used between different sizes of non-profit organisations and charities as defined in the Australian Charities Report. The sizes of charities were calculated on the basis of annual revenue and defined as follows:

- Extra Small (annual revenue below \$50,000);
- Small (annual revenue between \$50,000 to \$249,999);
- Medium (annual revenue between \$250,000 and \$999,999);
- Large (annual revenue between \$1,000,000 and \$9,999,999);
- Extra Large (annual revenue between \$10,000,000 and \$99,999,999); and
- Extra Extra Large (annual revenue of \$100,000,000 and above).

Average employee expenses per organisation were then calculated for each size category in each State and Territory.

Further, a national average payroll tax threshold for 2015/16 was calculated using the methodology specified in the 2015 Review; an average was taken of actual State and Territory payroll tax thresholds in place during that financial year, weighted by the total CoE paid in each State and Territory.

The employee expenses per organisation below the national average payroll tax threshold were then removed from the total employee expenses of charities and non-profit organisations to give employee expenses of charities and non-profit organisations above the average threshold in each State and Territory.

An adjusted revenue base was then calculated by subtracting non-profit and charity employee expenses above the average threshold from taxable private sector CoE.

Actual payroll tax revenues for 2015-16 were taken from the 2018 Update's Adjusted Budget. From the actual revenues, taxable private sector CoE and the adjusted base, effective national tax rates were calculated for both the original base (taxable private sector CoE) and the adjusted base (excluding charities and non-profit organisations).

By applying the corresponding national average effective tax rates to the original base and the adjusted base, assessed revenues were calculated for each State and Territory, both in terms of total dollars and dollars per capita, as well as the total level of redistribution and effective relativities for each State and Territory.

On the basis of this calculation, the ACT has found that adjusting the payroll tax base to account for the common exemption of charities and non-profit organisations from payroll tax would result in a material change to the GST distribution; with the ACT receiving approximately \$28.2 million, or \$70.75 per capita, in additional GST; well above the Commission's \$30 per capita materiality threshold. At a national level, the total amount of redistribution from this change would increase by approximately \$276 million, or \$11.49 per capita (Table D.4). For further information on the calculations, please refer to Attachment A.

**ACT GOVERNMENT RESPONSE ON COMMONWEALTH GRANTS COMMISSION 2020
REVIEW DRAFT ASSESSMENT PAPERS**

Table D.4 – Change in GST distribution from adjusting payroll tax base for exemptions to charities and non-profit organisations, 2015-16.

Data	National	NSW	VIC	QLD	WA	SA	TAS	ACT	NT
Original Assessed Revenue (\$m)	22,568	7,727	5,385	4,066	3,351	1,170	291	306	272
Original Redistribution (\$pc)	62.55	-65.92	56.81	95.27	-373.59	254.28	375.16	173.09	-173.11
Adjusted Assessed Revenue (\$m)	22,568	7,832	5,328	3,954	3,445	1,167	303	278	260
Adjusted Total Redistribution (\$pc)	70.38	-79.72	66.15	118.55	-410.55	256.00	351.87	243.85	-124.06
Change in GST Redistribution (\$m)	188	-106	57	112	-94	3	-12	28	12
Change in GST Redistribution (\$pc)	7.84	-13.79	9.34	23.29	-36.96	1.72	-23.29	70.75	49.05

Source: Commonwealth Grants Commission ASOL, Australian Charities Report and ACT Treasury calculations

On this basis, the ACT considers that adjusting the payroll tax base to account for the common exemption of charities and non-profit organisations from payroll tax would result in a material change to the GST distribution and improve the accuracy and adherence to the HFE principles of the Payroll Tax assessment. Thus, the ACT recommends that the Commission include this adjustment in its Payroll Tax assessment methodology for the 2020 Review.

LAND REVENUE

Summary

The Land Revenue assessment captures revenues from levies and taxes that are applied on land owners.

The ACT is supportive of the Commission staff proposals, including expanding the Land Revenue assessment to include revenues from parking space levies. The ACT considers that this proposal improves the accuracy of the assessment and its consistency with *What States Do*.

The ACT broadly supports the Commission staff proposal to continue to assess Land Revenue capacity on the basis of land values, including the proposal to continue to assess land tax capacity on the basis of land values, adjusted for land tax progressivity and State and Territory policies on aggregation. The ACT does note however that parking space levies are not charged on the basis of the value of parking spaces, but rather on the location of the spaces.

Further, the ACT notes that general property taxes and revenue generated from income producing properties are generally both charged on the basis of property values. Noting this, the ACT does not consider that there is a practical basis for the separation of the two sources of Land Revenue and proposes that they be combined into a single category of Land Revenue and assessed differentially.

However, the ACT considers an assessment of the revenue replacement amount from abolishing stamp duty should be discontinued.

Context

The Land Revenue assessment captures revenues from levies and taxes that are applied on land owners. Such taxes include land tax, property-based FESLs, metropolitan levies and the ACT's replacement revenue for Stamp Duty on Conveyances from general rates. Land Revenue does not include revenue from stamp duty, which are assessed in the Stamp Duty on Conveyances assessment, or revenues from planning and development levies and parking space levies.

Under the 2015 Review methodology, Land Revenue is assessed on the value of taxable land holdings in each State and Territory, separated between properties which produce incomes and general property taxes. Land tax capacity is assessed on the basis of the value of income producing land in each State and Territory by value range, accounting for the fact that most land taxes are only applied on commercial, industrial or residential investment property. All other Land Revenue sources are assessed on an EPC basis.

Land Revenue redistributed \$64 million, or \$154 per capita in GST funding to the ACT in the 2018 Update.

Commission Staff Position

Commission staff, in Draft Assessment Paper 2018-01/03-S, propose a small expansion of the 2015 Review methodology to include more types of Land Revenue. Outside of this expansion, the methodology is proposed to remain largely the same.

Commission staff propose to assess all land based taxes in the Land Revenue assessment other than those deemed to be user charges. Commission staff have identified planning and development levies as being user charges. Thus, compared with the 2015 Review methodology, Commission staff are effectively proposing to expand the types of revenue included in the Land Revenue assessment to incorporate parking space levies. The Commission staff proposal also includes the ACT's replacement revenue, provided the ACT is able to provide an estimate of how much general rates revenue is a replacement for stamp duty revenue, as well as property based FESLs. Capacity for Land Revenue is proposed to continue to be assessed on the basis of land values for residential, commercial and industrial properties.

Commission staff also propose to continue to assess land tax capacity on the basis of land values adjusted for the scope of taxation, excluding land used for primary production, general government and charities and for principal places of residence. Land values are proposed to be further adjusted for land tax progressivity and, if possible, State and Territory policies on aggregation, including the treatment of jointly owned land. Commission staff further propose to not assess foreign owner surcharge revenues separately, but to incorporate them into the land tax assessment and thus increase effective land tax rates in the Commission's assessment.

In addition, Commission staff seek views on what the most appropriate data source for land value data is and what adjustments would be necessary to ensure comparability between the States and Territories.

Commission staff also note the ongoing tax elasticity consultancy and recommend that a decision on a tax elasticity adjustment be deferred until the completion of the consultancy. Further, Commission staff recommend deferral of a decision on whether to discount the Land Revenue assessment until the assessment method has been finalised.

ACT Position

The ACT supports all the Commission staff proposals.

The ACT considers that expanding the Land Revenue assessment to include revenues from parking space levies improves the accuracy of the assessment and, while likely to have a small impact on the assessment and thus GST distribution overall, is more consistent with the principle of *What States Do*. The ACT notes that generally, we are supportive of minimising the number of revenue sources included in the Other Revenue assessment.

Further, the ACT notes that our Safer Families Levy is not currently captured by the Land Revenue assessment and is not reflected in Tables 4 and A-7 of the Draft Assessment Paper. The Safer Families Levy is an annual flat \$30 charged to every household in the ACT for the purpose of funding community support and awareness programs for domestic violence. It is the ACT's view that the Safer Families Levy falls within the purview of a land tax charged for State and Territory government functions and thus should be included in the assessment of the ACT's Land Revenue capacity.

With regard to the maintenance of the 2015 Review methodology of separating general property taxes from revenue generated from income producing properties, the ACT highlights that most general property taxes, including FESLs and metropolitan improvement levies, are charged at least in part on the basis of property values. This means that both general property taxes and revenue generated from income producing properties have the same tax base.

Noting this, the ACT does not consider that there is a practical basis for the separation of the two Land Revenue sources. The ACT proposes that general property taxes and revenue generated from income producing properties be combined into a single category of Land Revenue and assessed differentially.

In relation to the replacement of stamp duty revenue through the general rates system, it is unclear why this revenue is assessed. The Commission's assessment of the ACT's capacity to raise stamp duty revenue is unaffected by the ACT Government's tax reform program (not considering the potential elasticity issues). For example, once stamp duty is fully abolished in the ACT, the Commission will still assess the ACT's capacity to raise stamp duty revenue, just as is the case with NT and land tax. We suggest that this revenue should no longer be assessed.

The ACT broadly supports the Commission staff proposal to continue to assess Land Revenue capacity on the basis of land values, noting that most land taxes are levied on the basis of property values. This support also extends to the Commission staff proposal to continue to assess land tax capacity on the basis of land values, adjusted for land tax progressivity and, if possible, State and Territory policies on aggregation, including the treatment of jointly owned land and excluding land used for primary production, general government and charities and for principal places of residence. The ACT considers that these adjustments are fair and more accurately capture the range of property types that are subject to land tax, making the assessment more consistent with the principle of *What States Do*.

As noted in the Draft Assessment Paper, land tax is calculated differently in the ACT compared to all other States and Territories. In the ACT:

- Land tax is based on each property owned by an investor, rather than aggregating the total value;
- There is no tax free threshold; and
- For multi-unit dwellings land tax is based on the total AUV of the land rather than the individual AUV of each unit.

The ACT notes that the approach to calculating land tax for units in the ACT is not reflected in Tables 4 and A-7 of the Commission's Draft Assessment Paper.

The ACT also notes that parking space levies are not charged on the basis of the value of parking spaces, but rather on the location of the spaces. In this regard, the ACT considers that land values are not a suitable revenue base for parking space levies. The ACT considers that the Commission should investigate other potential revenue bases on which to assess parking levy capacity, such as the physical size of city central business districts as an example. If a suitable alternative revenue base cannot be identified, the ACT considers that parking space levies should be assessed on an EPC basis.

The ACT does not however support the Officer Working Party approach to the issue of the most appropriate source of land value data and the associated discounting of the Land Revenue assessment. Following the receipt of State and Territory submissions, Commission staff should review this issue and make final recommendations. The ACT will consider this issue further and include its response in a supplementary submission.

**ACT GOVERNMENT RESPONSE ON COMMONWEALTH GRANTS COMMISSION 2020
REVIEW DRAFT ASSESSMENT PAPERS**

The ACT also supports the Commission staff proposal to defer a decision on applying a tax elasticity adjustment to the Land Revenue assessment until the completion of the ongoing tax elasticity consultancy.

STAMP DUTY ON CONVEYANCES

Summary

The Stamp Duty on Conveyances assessment comprises revenue from stamp duties imposed on the transfer of property ownership and motor vehicles ownership.

The ACT is supportive of all of the Commission staff proposals for the Stamp Duty on Conveyances assessment, which we note are broadly consistent with the 2015 Review methodology.

The ACT does however propose to differentially assess revenue from sales of major State and Territory assets. We consider that RABs could be used as a policy neutral indicator of State and Territory revenue capacities, with a differential assessment occurring if the sale of a major State or Territory asset generated revenues that are greater than would be expected based on the RAB of the asset.

Context

The Stamp Duty on Conveyances assessment comprises revenue from stamp duties imposed on the transfer of property ownership and motor vehicles ownership. The concept of property comprises both real and non-real property.³ The duty payable is based on the value of the property transferred and is paid by the purchaser.

The assessment excludes:

- Taxes on land ownership, which are assessed in the Land Revenue assessment;
- Revenue from other stamp duties (such as stamp duty on the transfer of marketable securities), which are assessed in the Other Revenue assessment; and
- Payments to and concessions for first home owners (such as FHOG payments and concessional duties offered to first home owners), which are assessed in the Housing assessment.

Stamp Duty on Conveyances is assessed in three components under the 2015 Review methodology:

- An EPC component, comprising revenue from duties on the sale of major State and Territory assets, corporate reconstructions and land rich transactions of listed companies;
- A property component, comprising revenue from duties on both real and non-real property transfers and concessions for first home owners⁴; and
- A vehicle component, comprising revenue from the duty on transfer of vehicle ownership.

³ Real property is land and buildings (including houses, apartments, shops and factories). Non-real property comprises property that is not land or buildings. Examples include non-fixed plant and equipment, receivables, goodwill, business assets, statutory licences, intellectual property, aquaculture leases, copyright, patents, partnership interests and options to purchase.

⁴ Stamp duty concessions for first home owners are added back to revenue to give a gross figure, with the concessions treated as expenses in the Housing assessment.

In the ACT, stamp duty is being abolished over a 20 year period, with the revenue being replaced through the general rates system. Stamp duty on commercial transactions of \$1.5 million and below was fully abolished from 1 July 2018, though a flat rate of five per cent has continued to apply. Finally, it was announced in the 2018-19 ACT Budget that stamp duty for all first home buyers who have an annual income below \$160,000 will be abolished from 1 July 2019.

Stamp Duty on Conveyances redistributed \$45 million, or \$108 per capita in GST revenue to the ACT in the 2018 Update.

Scope of Assessment

Commission Staff Position

Staff propose to recommend the Commission include in the assessment:

- Revenue from duties on the transfer of real and non-real property, including foreign owner surcharges; and
- An amount equal to the concessional duty provided to first home owners.

Commission staff have yet to consider whether taxes on the transfer of motor vehicle ownership should be assessed and reported in a Stamp Duty on Conveyances assessment or in the Motor Taxes assessment.

ACT Position

The ACT supports the two Commission staff proposals.

With regard to foreign owner surcharges, the ACT supports the inclusion of these surcharges in the Stamp Duty on Conveyances assessment. Given that surcharge revenue is driven by the value of the underlying transactions, as for stamp duty, it appears that a separate assessment would not produce a different result from a combined assessment. Moreover, combining the two elements of revenue removes the need for a specific data collection on foreign owned property. However, if a separate assessment for the foreign owner surcharges were to be implemented, the required data should be available from the National Register of Foreign Ownership of Land Titles, which was established on 1 July 2016.

While strictly speaking the impact of combining the foreign owner surcharges with the main assessment does not introduce additional progressivity to the tax regime, it does increase effective rates across the value range and it may be that foreign purchases tend to be of higher value properties than the average.

The ACT has previously supported the add-back of stamp duty concessions for first home owners to assessed revenue to produce a gross revenue figure and the inclusion of the concessions as an expense in the Housing assessment. We continue to support this approach as being more transparent and accurate than including only a net revenue figure under the conveyance stamp duty head. It is also in accordance with government reporting of tax expenditures. In addition, we consider that concessions, such as those for pensioners or seniors, should also be added back to further refine the gross revenue figure, to the extent these concessions are common across the States and Territories.

With regard to stamp duty on motor vehicle transfers, the ACT considers that this revenue should be assessed as part of the Motor Taxes assessment.

The tax bases of property and motor vehicles are quite different and future directions for tax reform suggest that vehicle transfer duty is more likely to be considered as part of road user pricing and related reforms rather than in the context of a general reform of transaction based taxes.

Drivers of Revenue Capacity

Commission Staff Position

Staff propose to recommend the Commission:

- Assess Stamp Duty on Conveyances using the value of property transferred;
- Adjust the value of property transferred; and
 - To remove values relating to non-real property, corporate reconstructions and sales of major State and Territory assets;
 - For the wider scope of unit trusts and commercial real property in selected States and Territories; and
 - For the progressivity of transfer duty.
- Assess duty from transactions on non-real property, corporate reconstructions and sales of major State and Territory assets in the EPC component.

ACT Position

The ACT supports all of the staff proposals, with the exception of that relating to sales of major State and Territory assets.

In relation to the adjustments of the value of property transferred, the ACT considers it is important to take into account the differences in composition and distribution of otherwise equivalent tax bases across the States and Territories. As noted in comments on the macro approach in the A Broader Assessment Approach chapter, the smaller States and Territories lack the very high value properties found in the larger States. This clearly reduces the relative ability of small States and Territories to raise revenue from property transfers. The assumption of flat rates of taxation across tax bases, with no thresholds or exemptions, does not recognise the differing capacity of taxpayers across the States and Territories to pay and hence, the differing capacities of the States and Territories to raise revenue.

Sale of Major State and Territory Assets

The ACT considers that the Commission should examine the potential for a differential assessment of stamp duty on the sale of major State and Territory assets, as far as the duty represents a tax dividend from super-normal returns on such sales.

This revenue is essentially stamp duty on the transfers – it does not refer to the capital proceeds of sales as the assets in question were operated as GBEs and thus did not form part of the General Government Sector i.e. they were already out of the scope of equalisation. The stamp duty revenue from such sales is currently assessed EPC as the Commission consider that it is too difficult to identify a policy neutral revenue base for a differential assessment.

However, recent privatisation of major State and Territory assets, such as the electricity transmission and distribution networks in NSW and ports in NSW and VIC, suggested that purchasers of the assets may have paid a price premium reflecting an above-normal rate of return. Consequently, above-normal revenue would have been earned from the transfer duties associated with these privatisations. If so, there would be a good case for differential assessment of that revenue, provided a policy neutral measure of the base can be determined.

The recent Grattan Institute report *Down to the Wire: A Sustainable Electricity Network* provides some good indicators of how such an assessment could be constructed. The key theme of this report is the assertion that the RABs of the transmission and distribution businesses in NSW and QLD have been over-valued, with consequent higher costs to consumers and should be either written down (where the assets are still in State or Territory Government ownership) or a rebate paid to consumers (where the assets have been privatised). Based on a technical assessment by Morgans Research, Grattan has stated (p.36 of the report) that the three NSW electricity businesses sold for amounts well over their RABs: Endeavour for 1.69 times the value of its RAB, TransGrid for 1.67 times and Ausgrid for 1.4 times.

NSW Budget Papers for 2016-17 and 2017-18 specifically identify the transfer duty revenue received from the electricity privatisations (NSW Budget Statement 2016-17, Chart 5.1, p.5-6; NSW Budget Statement 2017-18, Chart 5.1, p.5-5) as \$455m for TransGrid in 2015-16 and \$489m for Ausgrid and \$229m for Endeavour in 2016-17. These years represent assessment years for the application years from 2017-18 to 2020-21 inclusive, so the latter two would still be relevant for the 2020 Review period.

The port privatisations in NSW (Port Botany and Port Kembla) occurred (were announced) in April 2013 and the 2017-18 application year would have been the last year for an assessment of the revenue from these sales to have been made, so they fall outside the timeframe of the 2020 Review. The Port of Melbourne privatisation was announced in September 2016 so would fall into the relevant timeframe but an examination of the VIC Budget Papers does not appear to give a figure for the transfer duty revenue from the sale.

The ACT's view is that the RABs are determined by independent regulators and thus constitute a policy-neutral measure of the asset bases and thus of the revenue bases relevant to the transfer duty payments. We do not propose exploring the issue of whether the RABs themselves are excessive, as it would be too difficult to identify an alternative policy neutral measure.

The transfer duty could not reasonably be assessed as part of the assessment of conveyance duty on property sales, in particular given the size and lumpiness of the privatisation transactions as well as the fact that they involve a qualitatively different type of asset, so they would have to form a separate component of the Stamp Duty on Conveyances assessment. All States and Territories could be expected to obtain a normal or market rate of return for privatising assets generally, so there would only be a case for differential assessment where States and Territories obtain above-normal returns. These can be characterised as windfall returns which were not generally available to other States and Territories.

The above-normal returns could be calculated as that portion of the transfer duty revenue above what would have been obtained if there had been no price premium on the asset sale i.e. if calculated on the basis of the RAB of the asset. This would give assessable amounts for the NSW electricity privatisations of:

TransGrid: \$183m ($\$455\text{m} \times 0.67/1.67$)

Ausgrid: \$140m ($\$489\text{m} \times 0.4/1.4$)

Endeavour: \$93m ($\$229\text{m} \times 0.69/1.69$)

These total \$183m assessable for the 2015-16 assessment year and \$233m assessable for the 2016-17 assessment year.

Given that the calculations are made on a policy neutral basis, the actual above-normal revenue can be considered as representing the additional revenue raising capacity of NSW accorded by the privatisations, i.e. an APC assessment is appropriate. Consequently, NSW would retain only a population share of the revenue, with the other States and Territories gaining population shares of the total. If this change to the assessments were to come in from 2020-21, as a result of the 2020 Review, it would only be the latter amount which would be gained. Although this would have only a one-year effect, the ACT considers that the principle is relevant to other asset privatisations by States which are not detailed here or may occur in the future.

The above numbers do not include the privatisation of the Ports of Melbourne and Darwin. Media reports indicate that the Port of Melbourne privatisation was worth \$9.7 billion, putting it well above the NSW Ports sale of \$5.07 billion and compared with \$10.3 billion for TransGrid and \$16 billion for Ausgrid. Investigation would also be required as to whether the regulatory regime for ports includes a concept similar to the RAB.

Elasticity Adjustment

Commission Staff Position

Staff propose to recommend the Commission defer consideration of an elasticity adjustment until it has considered the consultant's report on elasticities.

ACT Position

The ACT supports the staff proposal. The consultants have completed an initial scoping report but have still to present a final report on elasticity adjustments to be applied to particular categories of State and Territory taxation.

A short background paper on tax elasticity is at [Attachment B](#).

INSURANCE TAX

Summary

The Insurance Tax assessment differentially assesses the ability of States and Territories to raise revenues from duties on insurance products. The insurance products considered are general insurance, CTP motor vehicle insurance and life insurance, along with duties earned from workers' compensation insurance and FESLs

The ACT supports the Commission staff proposal to retain the 2015 Review methodology. We also support the proposal to assess workers' compensation in the Insurance Tax assessment, as we contend that it reflects *What States Do* and makes the Insurance Tax assessment more transparent.

Context

As a part of its revenue assessments, the Commission calculates the capacity of States and Territories to raise revenue from different duties on insurance products, inclusive of FESLs. These duties are imposed on insurance companies and passed on to consumers.

In the 2015 Review, the Commission assessed duties from general insurance (i.e. homeowner/motor vehicle/fire/public and product liability, professional indemnity insurance), CTP motor vehicle insurance and life insurance on a revenue base calculated using data from APRA on the total premiums paid for general insurance and CTP insurance in each State and Territory (the latter, wherever it was underwritten by private insurers).

This is supplemented by data from public insurers on total CTP insurance premiums. Premiums paid towards workers' compensation insurance were excluded from the revenue base, since while those premiums accounted for about 20 per cent of all insurance premiums, they contributed only two per cent of the insurance tax revenues. A separate assessment of duties from workers' compensation insurance was not material and hence, the Commission assessed such duties on an EPC basis in the Other Revenue assessment.

As NSW and TAS impose FESLs on insurance companies⁵ (which are in turn passed on to consumers), their premium data includes insurance based FESLs. The Commission ensures that NSW and TAS are not considered to have a higher revenue capacity to raise insurance taxes due to their policy choice of imposing FESLs on insurance companies. Hence, the value of insurance based FESLs are deducted from the premium data of NSW and TAS and the revenues collected from insurance based FESLs are assessed on the revenue base of general insurance premiums.

The Insurance Tax assessment redistributed \$4 million, or \$9 per capita in GST revenue to the ACT in the 2018 Update.

Commission Staff Position

Commission staff, in their Draft Assessment Paper CGC 2018-01/05-S, consider that the current assessment process achieves HFE and propose to recommend to the Commission that it is retained, with one minor change.

⁵ Other States and Territories impose FESLs based on land values.

Instead of workers' compensation duties being assessed separately in the Other Revenue assessment, Commission staff propose to assess it in the Insurance Tax assessment, using general insurance premiums as the revenue base.

ACT Position

The ACT supports the Commission staff position.

The ACT contends that the Commission staff recommendation of assessing workers' compensation duties in the Insurance Tax assessment reflects *What States Do*. The ACT also considers the proposal to use general insurance premiums as the revenue base for the assessment of workers' compensation insurance to be sensible since the latter accounts for 20 per cent of all insurance premiums but only two per cent of insurance tax revenues.

Further, the ACT notes the Commission staff comment that assessing workers' compensation insurance duties in the Insurance Tax assessment using general insurance premiums as the revenue base would not materially change the previous EPC assessment of those duties.

However, the ACT considers that such treatment would enhance the transparency of the insurance tax assessment, another factor behind the ACT's support for the Commission staff recommendation.

The ACT also supports the Commission staff recommendation of retaining insurance based FESLs in the insurance tax assessment as again, that is a reflection of *What States Do*, is consistent with the average policy approach adopted in the 2015 Review and also makes the assessment transparent.

MOTOR TAXES

Summary

The Motor Taxes assessment equalises the revenue generated by States on fees and charges relating to the ownership of vehicles, including vehicle registration fees, number plate fees, fire and emergency services fees levied on vehicles, traffic improvement fees and revenues from the Commonwealth Government's Federal Interstate Registration Scheme.

The ACT supports the Commission staff position to retain the 2015 Review methodology for the Motor Taxes assessment. We also support the Commission staff proposals to move stamp duty on vehicle transfers into the Motor Taxes assessment and for further investigation into updating the split of heavy and light vehicles. The ACT further supports the investigation into incorporating progressive rates of stamp duty on vehicle transfer into the assessment.

Context

The Motor Taxes assessment equalises the revenue generated by States and Territories on fees and charges relating to the ownership of vehicles. These fees include vehicle registration fees, number plate fees, fire and emergency services fees levied on vehicles, traffic improvement fees and revenues from the Commonwealth Government's Federal Interstate Registration Scheme. As per the 2015 Review methodology, motor taxes is not inclusive of stamp duty on vehicle transfers, driver licence and permit fees or duty on compulsory third part insurance. Under the 2015 Review methodology, these items are assessed under the Stamp Duty on Conveyances, Other Revenue and Insurance Tax assessments respectively.

Under the 2015 Review methodology, motor tax revenue capacity is assessed on the basis of the number of registered vehicles in each State and Territory. The number of vehicles is split between light and heavy vehicles, which accounts for States and Territories imposing significantly higher registration fees on heavy vehicles than on light vehicles. The current State and Territory splits on light and heavy vehicles are based on data from the 2009 Update.

The Motor Taxes assessment redistributed \$24 million, or \$57 per capita in GST funding to the ACT in the 2018 Update.

Commission Staff Position

Commission staff, in draft assessment 2018-01/06-S, have identified no major issues in the assessment methodology for motor taxes and propose to retain the 2015 Review methodology for the Motor Taxes assessment.

Commission staff also propose to move stamp duty on vehicle transfers from the Stamp Duty on Conveyances assessment. This is a presentational issue and would have no impact on the distribution of the GST.

Commission staff have indicated that they are working with State and Territory governments to update the split of heavy and light vehicles from new State and Territory data. Commission staff have also indicated that they are investigating incorporating progressive rates of stamp duty on vehicle transfer into the assessment.

Further, Commission staff have indicated their intention to harmonise the treatment of motor tax concessions with the treatment of stamp duty on conveyances concessions provided to first home buyers by treating the motor tax concessions as expenses rather than foregone revenue. Commission staff plan to investigate the impact of motor tax concessions on State and Territory budgets and possible policy neutral drivers of expenses.

Commission staff have also indicated that a possible elasticity adjustment to the Motor Taxes assessment is being considered as part of the ongoing tax elasticity consultancy. Possible elasticity adjustments on State and Territory revenue sources will be addressed when the consultancy is completed at a later date.

ACT Position

The ACT supports the Commission staff position to retain the 2015 Review methodology for the Motor Taxes assessment.

The ACT supports the Commission staff proposal to update the split of light and heavy vehicles for the 2020 Review. The ACT does consider however that, if States and Territories are able to consistently and reliably provide relevant data, the Commission should consider adjusting the methodology such that the split of light and heavy vehicles is updated as part of each annual Update in order to maximise the accuracy and contemporaneity of the Motor Taxes assessment.

The ACT further supports the Commission staff proposal to further investigate the harmonisation of the treatment of concessions on Motor Taxes and stamp duty concessions for first home buyers by treating Motor Tax concessions as expenses. The ACT considers that concessions are a State and Territory expense and conceptually should not be treated as foregone revenue. Additionally, the ACT supports the ongoing investigation into incorporating progressive rates of stamp duty on vehicle transfer into the assessment.

The ACT supports the Commission proposal to move transfer duties on vehicles into the Motor Taxes assessment. The ACT considers that as these revenues are related to motor vehicles, it is more transparent for them to be assessed under the Motor Taxes assessment. The ACT also supports the Commission staff intention to investigate the incorporation of progressive transfer duties on vehicles.

The ACT also notes that reforms to user charging for roads over the coming years could potentially alter the Motor Taxes assessment by bringing what are currently vehicle registration fees and possibly other elements of the Motor Taxes assessment under the purview of the Roads assessment as user charges.

GAMBLING TAXES

Summary

Gambling tax revenue was assessed EPC in the 2015 Review. Commission staff are investigating options for introducing either a disaggregated or aggregated differential assessment of gambling tax revenue in the 2020 Review. They intend to further investigate the results from a HILDA survey as the basis of the former and, alternatively are considering the use of high level indicators (e.g. GHDI) to investigate the latter approach. If neither approach results in a material assessment, then they intend to continue with an EPC assessment in the 2020 Review.

The ACT encourages Commission staff to continue with their investigations of a differential assessment of gambling taxation revenue which would improve the HFE outcome. To assist in this process, the ACT has developed a draft aggregated differential assessment using socio-demographic drivers of gambling identified from the HILDA survey data which could be explored further by Commission staff.

Context

Gambling taxes comprise revenue from a mix of direct taxes on various forms of gambling, licence fees and other contributions. The main forms of gambling taxes are racing taxes, lottery taxes, gaming machine taxes, casino taxes and sports betting taxes. According to the ABS' taxation revenue publication (Cat. No. 5506.0), States and Territories collected a total of \$6.1 billion from gambling taxes in 2015-16, which, on average, was 4.7 per cent of their own-source revenues.

However, the proportion of States' and Territories' own-source revenues from gambling taxation varies significantly by State and Territory. In 2015-16, it ranged from a low of 1.2 per cent for WA to a high of 6.4 per cent for the NT. 1.8 per cent of the ACT's own-source revenues came from gambling taxes, the second-lowest in Australia.

There are major differences in State and Territory policies with regard to raising revenue from gambling activities.

- WA does not allow gaming machines outside of its single casino, e.g. in clubs and pubs, whereas the ACT has only recently allowed electronic gaming machines in its casino, with some restrictions.
- There are vastly different tax regimes for different types of gambling across the States and Territories.
 - Tax rates on lotteries vary from 40 per cent to over 70 per cent.
 - SA has introduced a point of consumption wagering tax on the net wagering revenue of betting companies from 2017-18 while the ACT, NSW and VIC will introduce it from 1 January 2019. Other States and Territories are likely to follow.
- Licence fees applied to gambling venues vary widely across States and Territories, with casinos in all States and Territories apart from the NT paying licence fees in addition to the relevant taxes.

Since the 2004 Review, the Commission has been unable to establish a conceptual case for a differential assessment of gambling revenues because it has been unable to identify the factors that drive gambling expenditure. Further, the commencement of online gambling has added to the complexity since the players being taxed could be from another State or Territory or even overseas.

- In the 2015 Review, gambling taxes were assessed EPC in the Other Revenue assessment. The Commission chose this approach because the effect of State and Territory policies meant it was unable to develop a policy neutral capacity measure for each form of gambling or a policy neutral broad assessment of all gambling that was material.

Gambling Taxation Assessment in the 2020 Review

Context

According to the Commission's assessment guidelines for the 2020 Review, an assessment will only be made when:

- A case for the assessment has been established;
- A reliable method has been devised;
- Data are available that are fit for purpose and of suitable quality; and
- The assessment is material.

Gambling taxes will continue be assessed EPC in the 2020 Review if the Commission is unable to develop an assessment that satisfies the four criteria above.

Thus, the case for a differential gambling assessment depends on:

- Identification of the underlying factors driving gambling expenditure;
- Development of a reliable method for the assessment of such factors; and
- Materiality of the assessment.

Commission staff note that the primary issues in developing an assessment method have mostly remained unchanged. They are:

- The degree of substitutability between various forms of gambling;
 - Low substitutability implies that each form of gambling may have to be assessed separately while high substitutability implies that a single assessment would be sufficient.
- The effect of State and Territory policies; noting if policy differences are material, adjustments may be required to amend or remove them from the chosen capacity measure; and
- The effect of differences in the propensity to engage in gambling.

In the 2015 Review, the Commission explored a range of research and noted different studies suggested different drivers of gambling activity. Further, it was unable to find reliable and comparable data that would enable it to link gambling activity to drivers beyond a State/Territory's control.

Commission staff have reviewed the latest literature on gambling research. They note the availability of a new study (by Armstrong and Carroll, Australian Gambling Research Centre, December 2017) that provides information on the characteristics of gamblers, making use of data from the HILDA survey. Questions on gambling activity have been added to the survey in the recent past (Wave 15 (2015) onwards), making HILDA a potential source of data the Commission could use to accurately identify the underlying drivers of gambling activity.

Commission staff have analysed Armstrong and Carroll's work and share the following results:

- Compared to the general Australian adult population, regular gamblers were more likely to be male, 50 years and older, either have 10 years or less of schooling or a certificate/diploma as their highest level of education, be retired, live alone or with their partner and no others outside a major city, and draw on welfare as their main source of income.
- Differences in SDC were related to different gambling activities.

At the same time, the Commission staff share some concerns about the limitations of HILDA data – possible lack of representativeness from low response rates and potential problems with response bias and recall. Further, they also contend that since the HILDA survey questions ask about gambling expenditure and activity in a typical month, it excludes one-off or occasional participation in gambling, implying that while it captures the socio-demographic profile of regular gamblers, it does not capture all gambling activity.

Finally, they also note that State and Territory policy differences could affect gambling activity through SDC effects. That said, Commission staff propose to continue exploring the HILDA data and investigating links between SDC and gambling activity.

Commission staff have investigated other population based measures such as household expenditure, number of people in population subgroups and proportion of people in high and low incomes in the past. Their past experience indicates that a population based measure would be unlikely to pass the Commission's disability materiality threshold of \$35 per capita, which makes that avenue of research less promising.

On the other hand, Commission staff indicate that a broader measure applied to an aggregated assessment is worth exploring further, as suggested by the high substitutability of various gambling forms and pervasiveness of State and Territory policies. Previously the Commission has used gambling expenditure, gambling turnover, GHDI and population as broad measures of revenue capacity.

However, Commission staff cite issues with the quality and reliability of gambling expenditure and turnover data sourced from QGSO. Further, their analysis presented in Tables 5 and 6 of the Draft Assessment Paper shows the assessment would be very sensitive to the choice of the broad measure since the revenue capacities of States and Territories vary markedly depending on the broad measure chosen.

In summary, Commission staff contend either a disaggregated or aggregated gambling assessment could be considered for the 2020 Review.

A disaggregated assessment, in which each form of gambling would have its own component, could be based on:

- The SDC of gamblers using HILDA data;
- The number of people in particular age groups, such as the population aged 15 and over; and/or
- The number of people in particular income groups, such as the number of people with low income or the number of people with high income.

However, Commission staff consider it will be difficult to develop a disaggregated gambling assessment for the 2020 Review. Due to the reasons mentioned above (high substitutability between gambling forms, etc.), they contend that an aggregated assessment based on one of the broader measures of revenue capacity the Commission has used in the past seems more promising.

Commission Staff Position

Staff propose to recommend the Commission:

- Continue to investigate a disaggregated gambling assessment based on HILDA data;
- Continue to investigate an aggregated assessment based on broad measures of gambling capacity; and
- Pending the outcome of these investigations, assess gambling taxes EPC.

ACT Position

The ACT encourages Commission staff to continue their investigations of a differential assessment for gambling taxation. In order to assist the Commission staff in further exploring a differential assessment, we have also analysed the Gambling Research Report and developed a possible differential assessment for gambling taxation. It is an aggregated assessment based on broad measures, with socio-demographic information identified through the HILDA survey data being used to determine revenue capacity.

Our proposal is structured accordingly:

- Introduction;
- The conceptual case;
- A reliable method;
- Data is fit for purpose and of a suitable quality;
- A material assessment;
- Conclusion; and
- References

Introduction

The Commission Staff Draft Assessment Paper *Gambling Taxes* (CGC 2018-01/07-S) and Staff Research Paper *What States Do - Gambling Taxation* (CGC 2017-09-S) highlight the current challenges with the gambling taxation assessment. Considering the policy neutrality challenges, the ACT suggests that use of a high level indicator, in combination with socio-demographic factors which indicate a propensity to gamble as outlined in the following sections, could be further explored to provide the basis of a policy neutral calculation of the revenue base.

The ACT considers that while challenges still remain in deciding whether State and Territory GFS data or statistics prepared by QGSO better reflects States' and Territories' gambling taxation revenues, the Commission is well equipped to resolve the issue. Hence, this proposal focuses solely on the determination of policy neutral revenue bases for the gambling taxation assessment.

A key driver for the proposal is the observation from CGC 2018-01/07-S (and previous Commission papers) that gambling taxation revenue amounts to a significant figure of \$6.1 billion (2015-16). The ACT argues that given the size of the revenue stream and wide variation across States and Territories, there is a strong case for developing a differential assessment. The ACT notes that the lack of a differential assessment of gambling taxation revenue is a significant source of criticism of the HFE system.

Conceptual Case

As mentioned above, in the 1999 and 2004 Reviews (and possibly earlier) the Commission calculated the gambling revenue base of the States and Territories using GHDI data, discounted by 50 per cent to take into account the fact there was no conclusive evidence that GHDI was the sole indicator of propensity to gamble. The ACT had concerns with such an approach on the basis there is no direct relationship between GHDI and propensity to gamble at all (i.e. a State or Territory with high GHDI does not necessarily have high gambling expenditure/turnover).

Some States and Territories also had issues with the level of discounting that was applied, which was a judgement of the Commission. Notwithstanding State and Territory concerns, a key factor for the use of GHDI was it enabled the Commission to carry out a policy neutral assessment. Thus, a key point to note is that **broad level income indicators can be policy neutral and if combined with valid indicators of propensity to gamble, which would overcome the need to discount based on judgement on the Commission's behalf, they can enable a credible differential assessment.**

Analysis of the HILDA survey data shows gambling participation happens across all segments of HDI, though there are socio-demographic traits which stand out. The ACT contends that total annual personal income by State/Territory can be treated as the revenue base of gambling taxation, with socio-demographic traits which are clear indicators of propensity to gamble used for the differential assessment of the revenue.

Tables 2.5 and 3.2 (pp. 13-14 and 21-22 respectively) available in the Gambling Research Report show the SDC associated with gambling participation and gambling expenditure in Australia.

A comparison of the percentage contribution of each socio-demographic group with its population share in the Australian adult population shows that:

- Males account for 49 per cent of Australia’s adult population while they account for 54.2 per cent of the population which regularly participates in gambling and contribute about 64 per cent of the total gambling expenditure. Thus the male gender group stands out as a socio-demographic differentiating factor.
- The age-group 30 and above accounts for 88.1 per cent of the Australian adult population which participates in gambling and about 87.5 per cent of total gambling expenditure, compared to just 77.5 per cent of the Australian adult population overall, indicating it is a strong candidate as a differentiating factor from a socio-demographic perspective.
- A similar comparison with regard to education level shows that 79.1 per cent of gambling participants do **not** have a Bachelors or higher degree. The same group account for 84.5 per cent of gambling expenditure. This compares to only 72.3 per cent of the Australian adult population not having Bachelors or higher degree. This suggests a clear indicator of gambling propensity.
- Comparisons using other factors (e.g. ‘Employment’) do not show any clear outliers which can be used as a differentiator.

A Reliable Method

Based on the findings above, it appears the population group identified as male, aged 30 or above who do not have a Bachelor’s degree or higher are more likely to engage in gambling activity compared to the rest of the Australian adult population.

Hence, the ACT considers the revenue base for gambling taxation assessment could be based on the **total annual personal income of male State residents aged 30 or above who do not have a Bachelor’s or higher degree**. We suggest ABS microdata could be used for determining the revenue base. The following ABS Census TableBuilder data items could be used to calculate the revenue base for each State and Territory for every assessment year that is a Census year. When the assessment years are non-Census years, ABS’ advice can be used to determine an appropriate index for each State and Territory.

- Setting each State and Territory as a column, the following would be chosen as rows:
 - Total personal income (weekly) (from \$1/week and above, ranges given by the ABS);
 - Gender being restricted to males;
 - Age (in ten-year groups) being restricted to the 30 or above age group; and
 - Highest educational attainment being restricted to those who do not have a Bachelor’s or higher degree.

The output in the Census TableBuilder would be the number of male State or Territory residents who are in the age-group 30 or above and who do not have a Bachelors or higher degree as their highest education status, and who earn income within the specific range available in the row of the table.

Considering there are 13 income-ranges in the ABS data, for any State or Territory, the total revenue base is given by:

$$\text{Total revenue base for any State/Territory} = \sum_{i=1}^{13} (\text{ave}_i * \text{MaleResPop}_i)$$

Where:

- i denotes an income range;
- ave_i denotes the mid-point of the income range i (which acts as a proxy for the average income for that income range); and
- $MaleResPop_i$ denotes the number of male State/Territory residents who are in the 30 or above age-group and who do not have a Bachelors or higher degree and whose annual income lies in the income range i :

Once the revenue base is determined, the assessment can proceed in the usual manner:

- A national average tax rate can be determined using the sum of actual gambling revenue data across the States and Territories divided by the sum of individual State and Territory revenue bases calculated above; then
- Assessed revenue for each State and Territory can then be calculated by multiplying the State/Territory's revenue base with the national average tax rate.

Attachment C shows the data for each State and Territory taken from ABS TableBuilder data on 2016 Census and an indicative assessment using the approach outlined above⁶.

Some aspects relevant to the proposed method are discussed below.

Policy Aspects

The Commission has often highlighted the widely differing policies across the States and Territories as a challenge in following the standard methodologies as applied in revenue assessments, in relation to the gambling taxation assessment. The ACT agrees and hence has proposed an approach for determining revenue capacity of the States and Territories using proxy measures. Since the approach uses socio-demographic measures of propensity to gamble and does not take into account State/Territories' gambling related policies, the calculation of revenue capacity of a State or Territory is likely to be policy neutral.

With many States and Territories moving towards a point of consumption tax for online gambling (with most other gambling taxes being applied at the point of consumption already), this alternative approach could be construed as a determination of point of consumption revenue capacity for all gambling activity in a State or Territory.

Problem Gamblers

The Gambling Research Report shows (p. 47) that non-problem gamblers accounted for 58 per cent of typical gambling expenditure in 2015 while the combined total of risk groups associated with gambling – low risk, moderate risk and problem gamblers accounted for 42 per cent of the expenditure.

Within the 'at risk' groups - low risk, moderate risk and problem gamblers accounted for 15 per cent, 17 per cent and 10 per cent of gambling expenditure respectively⁷.

⁶ Note that as the data for States' and Territories' gambling taxation revenue is not available beyond 2015-16, the data obtained from ABS TableBuilder, while for 2016-17, has been assumed to be that for 2015-16 in order to show an indicative assessment.

However, considering that the socio-demographic driver chosen for gambling - males in the age-group 30 or above who do not have a Bachelor's or higher degree as their highest education status - was chosen on the basis of overall gambling participation and expenditure, it is unsurprising that analysis of the SDC of risk groups (p. 34) shows that low risk and moderate risk groups of gamblers have practically the same profile as the one chosen for a differential assessment. We acknowledge that SDC of problem gamblers may fall in a different group (e.g. the age group 18-29 cannot be excluded in that scenario), but considering they account for only 10 per cent of total expenditure and a much lesser proportion in relation to participation, we suggest that the proposed approach is typical of most gamblers.

The PC Inquiry Report on Gambling (No. 50, 26 February 2010) estimated that problem gamblers accounted for 40 per cent of all gaming machine revenue (which in itself was an average of a very wide range of 20 per cent to 60 per cent). The latter in turn accounted for about 62 per cent of all gambling expenditure⁸, indicating that at least 25 per cent (40 per cent * 62 per cent) of all gambling expenditure was from problem gamblers **at that time**. While strictly not comparable due to the manner in which gambling expenditure has been derived in the Gambling Research Report, the latter contends that the current contribution for problem gamblers is only 10 per cent. We note the PC report, *inter alia*, mentions that:

- The gambling industry was maturing in the 2000s, showing a slower rate of growth and lower prevalence rates;
- Outcome and client follow-up data for support services show significant decreases in clients' involvement in gambling and their gambling-related problems following treatment; and
- Gambling expenditure by problem gamblers was on a downward trend in comparison to the PC's report in 1999.

Hence, we consider the fall in contribution of problem gamblers to overall gambling expenditure, as indicated by the Gambling Research Report, is not unexpected.

Use of Total Annual Personal Income Derived from Total Weekly Personal Income Data

The ACT agrees with the concerns identified in earlier Reviews about whether an indicator as broad as GHDI was an appropriate measure of the gambling taxation revenue base. Likewise, a similar concern could be raised about the use of total annual personal income. However, the ACT contends that this concern has been mitigated by the following consideration:

- While, like the GHDI, total annual personal income is a broad revenue base, the fact that ABS' Census TableBuilder allows us to directly determine the total number of people whose socio-demographic characteristics show a higher propensity to gamble, hence allowing us to derive the total annual income of such groups, mitigates the broad revenue base concern. Moreover, there is no discounting required in this case since data on the relevant socio-demographic groups with higher propensity to gamble are being used directly.

⁷ ACT Treasury calculations based on data in p.47. Share of low risk gamblers = $1302 / (4963 + 1302 + 1478 + 853) = 15$ per cent. Similarly share for moderate risk gamblers = 17 per cent and share for problem gamblers = 10 per cent.

⁸ Inclusive of spending in clubs, pubs and casinos.

The ACT recommends the mid-point of the weekly/annual income range be used to calculate the total personal income of people who have a higher propensity to gamble and whose income falls within that weekly/annual income range. Ideally, the average figure of a particular income range would have been the best to use in such a circumstance. However, the average value is not available since State and Territory residents respond to the ABS' survey with their household income ranges and not specific values (e.g. \$1-149 per week as opposed to \$125 per week).

Alternatively, the median value of that income range could also have been used. However, discussions with the ABS revealed very little differences between the choices of mid-point of the income range and median value of the income range, with the former having the advantages of being much simpler and no dependency on the ABS. Hence, the ACT's preference to the mid-point of the income range as a proxy for the average value of the income range to calculate the total annual personal income of the specific population groups by State and Territory.

Single or Multiple Assessments for Different Types of Gambling

A key consideration in deciding whether a single assessment is sufficient for gambling taxation is whether the drivers of various forms of gambling are significantly different from each other. In other words, a low level of substitutability among various forms of gambling would indicate they have different drivers and hence, ideally, different assessments should be used for each form of gambling (as done in the case of mining revenues, for example). On the other hand, a high level of substitutability among various forms of gambling would indicate they have similar drivers and a single assessment for the category would be sufficient.

Tables 2.3 and 2.4, p. 12 of the Gambling Research Report aids in determining the level of substitutability among various forms of gambling. Table 2.3 indicates that among the major forms of gambling, lottery was the gambling activity in which 59.3 per cent of regular gamblers participated on a sole activity basis, while for all the other major activities (EGMs, instant scratch betting, race betting etc.) the figure was less than 30 per cent. This suggests that there is a case for assessing lotteries on an individual assessment basis, while the other major forms of gambling can be considered to be substitutable.

However, given that 40.7 per cent of lottery players participated in at least one other gambling activity and such players are spread across all the different forms of major gambling activities (Table 2.4, p. 12), it appears that the drivers of lottery participation are not significantly different from the drivers of participation in other forms of gambling, i.e. lottery as a form of gambling can be considered to be substitutable with the other forms of gambling.

Thus, all the major forms of gambling activities can be considered to be substitutable. As a result, the ACT considers that a single assessment would be sufficient for gambling taxation revenues.

The ACT notes the Gambling Research Report does highlight that there are clear patterns in terms of socio-demographic groups that participate in some forms of gambling. Moreover, socio-demographic groups excluded from this proposal, like the 18-29 age-group, participate heavily in gambling activities like sports betting. Thus, an individual assessment for various forms of gambling *could* have been considered. However, that would make the assessment extremely complex.

Further, the gambling taxation revenues from activities in which the excluded groups participate are so small that any difference is not likely to be material. Hence, apart from the substitutability reasons cited above, on simplicity grounds, the ACT would suggest a single assessment for gambling taxation, as opposed to multiple assessments for various forms of gambling.

Regression of Gambling Expenditure Using the Proposed Revenue Base as the Independent Variable

As mentioned above, this alternative approach for a differential assessment of gambling taxation revenue is based on total annual personal income of male State or Territory residents who are aged 30 or above and who do not have a Bachelor’s or higher degree as their highest education status as the revenue base for that State or Territory. In order to check whether this revenue base has a significant relationship with gambling expenditure in that State or Territory, we estimated a simple linear regression using gambling expenditure as the dependent variable and the revenue base as the independent variable. The regression results are shown in Figure D.1⁹.

Figure D.1: Regression results of gambling expenditure against proposed revenue base

Dependent Variable: SERIES03				
Method: Least Squares				
Date: 06/28/18 Time: 20:25				
Sample: 1 8				
Included observations: 8				
Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	-592.5944	552.0716	-1.073401	0.3244
SERIES01	0.105953	0.014550	7.282043	0.0003
R-squared	0.898354	Mean dependent var		2473.120
Adjusted R-squared	0.881413	S.D. dependent var		2933.305
S.E. of regression	1010.129	Akaike info criterion		16.88586
Sum squared resid	6122160.	Schwarz criterion		16.90572
Log likelihood	-65.54344	Hannan-Quinn criter.		16.75191
F-statistic	53.02814	Durbin-Watson stat		0.920773
Prob(F-statistic)	0.000342			

From the regression results above, we observe that both the model and revenue base as the independent variable are statistically significant at the five per cent level. Further the value of the adjusted R-square (88.1 per cent) indicates that variations in the revenue base (i.e. the independent variable) explain 88.1 per cent of the fluctuations in gambling expenditure. Further the coefficient of revenue base is positive, implying a positive correlation between gambling expenditure and the revenue base of this approach, which aligns with our expectations.

Hence, the regression results demonstrate a statistically significant relationship between gambling expenditure and the recommended revenue base.

⁹ The regression results show the standard errors with correction for heteroskedasticity.

Fitness for Purpose of Data

Gambling Expenditure by Tourists against State and Territory Residents

An important factor from the perspective of the gambling taxation revenue assessment is the revenue collected from tourists since such revenues, especially from international tourists, would not be covered in the HILDA survey report.

Analysis of State Tourism Satellite Accounts data from Tourism Research Australia shows that tourists' consumption of gambling and betting services is a minor percentage of total gambling expenditure. For 2014-15, domestic and international tourists were responsible for just 6.4 per cent of total gambling expenditure in Australia (total consumption of gambling and betting services by tourists was \$1.466 billion vis-à-vis total gambling expenditure of \$22.75 billion across Australia)¹⁰.

Moreover, while international tourists are excluded from the HILDA survey, domestic tourists with a propensity to gamble are included. Table D.5 below shows the contribution of international tourists relative to the overall consumption of recreation, cultural and gambling services (by all tourists) has varied from 15 per cent to 17.3 per cent between 2009-10 and 2016-17. Applying a similar percentage to the gambling consumption by all tourists (e.g. \$1.466 billion in 2014-15), shows that consumption of tourists whose data would not have been captured by the HILDA survey is less than 1.5 per cent of total gambling expenditure, a negligible figure for all practical purposes.

Table D.5: Consumption of recreation, cultural and gambling services by international tourists

Item	2009-10	2010-11	2011-12	2012-13	2013-14	2014-15	2015-16	2016-17
Recreation, cultural and gambling services consumed by domestic tourists (\$ million)	4,397	4,499	4,676	4,820	4,784	5,060	5,061	5,328
Recreation, cultural and gambling services consumed by international tourists (\$ million)	815	852	830	839	861	913	1,024	1,117
Percentage consumed by international tourists (per cent)	15.64	15.92	15.07	14.83	15.25	15.29	16.83	17.33

Source: ABS 5249.0, Table 10

Sensitivity Analysis on the Highest Total Weekly Personal Income Range

As indicated above, for calculating the total income earned by State and Territory residents in a particular income range, the ACT recommends the use of the mid-point of the income range (available in ABS total personal income (weekly) series) as a proxy for the average of the income range. As an example, for the annual income range \$1-\$7,999, the value of income to be used is the average of \$1 and \$7,999 (i.e. \$3,800). A similar method can be used for each income range except the highest - the range from \$156,000 and above.

Since a specific figure other than \$156,000 is not available, the ACT suggests for the highest income range, \$156,000 is used.

¹⁰ The same figure was 6.8 per cent for 2015-16 (the final year for which data is available in Australian Gambling Statistics 1990-91 to 2015-16, 33rd edition published by the QGSO).

Discussions with the ABS revealed the median of the highest income range is \$3,996 per week, i.e. \$207,792 annually. Using an annual income value of \$208,000 in lieu of \$156,000 does not have a material impact on the assessment.

Comparison of Household Income and Labour Dynamics in Australia data to Other Gambling Statistics

Appendix A in the Gambling Research Report shows comparisons between estimates produced from the HILDA data and estimates produced from other national and State/Territory specific studies. The biggest advantage of using the HILDA survey estimates is the survey uses a representative sample of the Australian population (as opposed to the focus on gamblers in the other national and State/Territory surveys) and hence, socio-demographic indicators from the survey could reliably be used as disabilities in the gambling taxation assessment.

When compared with other surveys, the HILDA survey has differences in expenditure and participation across various forms of gambling. However, as various forms of gambling have been considered to be substitutable, such differences across forms of gambling are not relevant.

Other differences between results from the HILDA survey and those from other surveys are also mentioned in Appendix A of the Gambling Research Report. A study of those differences reveals that apart from the contribution to gambling expenditure by tourists, in ACT's view, none of the other differences indicate a better approach compared to the use of the HILDA survey results for gambling taxation assessment.

In a similar vein, the ACT notes the concerns Commission staff raise in the Draft Assessment Paper CGC 2018-01/07-S about the reliability of using HILDA survey data for a differential gambling assessment. While there is a possibility there would be some issues with response bias and recall (possibly true for most surveys), we contend such issues would likely impact only a small number of the total responses to the HILDA survey. We note the Commonwealth Government has often used HILDA survey data for framing policies including proposals on Australia's Future Tax System Review, the 2011 Paid Parental Leave Policy, decisions on minimum wage rates and national monetary policy¹¹. In addition, the HILDA survey is regarded as one of the best panel surveys in the world.

Commission staff also express concerns that one-off gambling is not captured in the HILDA survey considering that the focus is on regular gamblers. We consider the concern to be minor given significant expenditure on gambling would likely originate from regular gamblers and not the one-off participants. There are advantages in the fact that the HILDA survey does not focus on one-off gamblers, as it makes clear the actual socio-demographic drivers of gambling.

Materiality

As the calculations in Attachment C show, the assessment would be material. The GST redistribution due to the proposed method has been reproduced in Table D.6 below.

¹¹ <http://www.ands.org.au/news-and-events/dataimpact/data-impact-stories/hilda-survey-shapes-policy-on-tax-and-jobs>

ACT GOVERNMENT RESPONSE ON COMMONWEALTH GRANTS COMMISSION 2020 REVIEW DRAFT ASSESSMENT PAPERS

Table D.6: GST redistribution due to the proposed assessment method

	NSW	Vic	Qld	WA	SA	Tas	ACT	NT	Redistribution
2015-16 (\$m)	104.08	113.37	-71.07	-145.18	-5.08	0.84	9.79	-6.75	228
2015-16 (\$pc)	13.55	18.59	-14.77	-56.91	-2.97	1.63	24.49	-27.62	0.00

We note that even with the proposed increased materiality threshold of \$35 per capita proposed in the 2020 Review, the assessment would be material.

Conclusion

While acknowledging that further research and analysis would be required, the ACT considers that the approach of using HILDA data provides a basis to resolving the challenges of determining policy neutral methods for assessing gambling taxation by making use of broad indicators like total annual personal income (derived from the total weekly personal income series), along with the use of socio-demographic factors which indicate a propensity to gamble.

We consider the HILDA survey data to be a reliable source for socio-demographic drivers of gambling which provides the basis for establishing the conceptual case for a differential assessment. Further, since the data needed for the assessment can be obtained from a reliable source like the ABS, which the Commission already relies on for data related to multiple assessments, the quality of data is high. The method followed is simple and intuitive, making good use of the advantages provided by ABS TableBuilder, providing the framework for a reliable assessment. On this basis, we consider the alternative method outlined in this section satisfies the Commission's criteria used in the 2020 Review for establishing a differential assessment.

The ACT suggests the approach presented in this proposal addresses many of the challenges with previous differential assessments of gambling taxation revenue and would welcome the Commission's views on whether this approach should be explored further.

References

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- Appendix State Tourism Satellite Accounts, 2014-15, Tourism Research Australia, <https://www.tra.gov.au/Research/View-all-publications/All-Publications/Economic-reports>
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MINING REVENUE

Summary

The Mining Revenue assessment captures revenues generated from royalties on mineral extraction. The Mining revenue assessment has been contentious for many years given inherent issues with *Policy Neutrality* and the impact it has on the overall GST distribution.

The ACT supports the Commission staff proposal to retain the 2015 Review assessment methodology. The ACT also supports the proposal to assess a portion of any additional revenue generated through a change in royalty rates on an EPC basis and considers the proposal to be an effective way of addressing concerns with *Policy Neutrality* in the assessment of minerals which have production dominated by one or two States or Territories.

The ACT also supports the Commission proposal to assess banned minerals on an EPC basis. The ACT considers the 2015 Review approach of assessing States and Territories that have banned development as having no capacity to generate revenue in relevant minerals is inconsistent with the principle of *Policy Neutrality*. Given the practical limitations of assessing banned capacity, the ACT considers that an EPC assessment is the most appropriate option.

Context

The Mining Revenue assessment captures revenues generated from royalties on mineral extraction. The assessment also includes Commonwealth Government grants paid in lieu of royalties for uranium and offshore gas and oil. Royalties from iron ore and coal dominate the assessment, representing 42 and 40 per cent of all assessed mining revenue respectively in 2016-17.

Under the 2015 Review methodology, mining revenue capacity is assessed on the basis of the value of mineral production. The assessment is performed on a mineral-by-mineral basis for iron ore, coal, gold, copper, bauxite and nickel, with all other minerals being assessed as a single category.

The Mining Revenue assessment has been contentious for many years given inherent issues with *Policy Neutrality*. Mineral resources are heavily concentrated in a small number of jurisdictions, chiefly WA, but also QLD and NSW for some minerals such as coal. Consequently, a national average policy approach to determining each State and Territory's revenue capacity from mining revenues effectively results in dominant producers determining the national average policy. The Mining Revenue assessment has also been contentious due to the effect the assessment has on the overall GST distribution. Because mining royalties are a major component of dominant mineral producing States' and Territories' revenues, large amounts of GST are transferred from dominant mining States and Territories such as WA to States and Territories with little or no mining capacity such as the ACT.

The Mining Revenue assessment redistributed \$188 million, or \$449 per capita of GST funding to the ACT in the 2018 Update.

Commission Staff Position

In Draft Assessment Paper 2018-01/08-S, Commission staff generally propose to maintain the 2015 Review assessment methodology. This includes continuing to assess State and Territory mineral royalties and Commonwealth Government grants in lieu of royalties under the Mining Revenue assessment and to continue to assess State and Territory mining revenue capacities on a free-on-board value of production basis. Commission staff further propose to continue to assess State and Territory mining revenue capacity on a mineral-by-mineral basis and to not adjust States' and Territories' assessed capacities for differences in development policies and compliance efforts.

Commission staff are proposing however to assess a portion of any additional revenue generated through a change in royalty rates on an EPC basis in order to address concerns with policy neutrality for dominant producer States and Territories making unilateral adjustments to their royalty rates. The Commission's proposed approach would result in 50 per cent of any additional revenue being assessed on an EPC basis.

Commission staff are also proposing to change how minerals which have moratoriums or bans on development placed on them are assessed. Under the 2015 Review methodology, States and Territories which have moratoriums or bans are assessed as having no revenue capacity for the relevant minerals. Commission staff are proposing instead to assess these minerals on an EPC basis on a national level.

Commission staff have also recommended that a decision on whether to apply a tax elasticity adjustment to mining revenues be deferred until the completion of the ongoing tax elasticity consultancy. Commission staff also recommend a deferral on deciding if the Mining Revenue assessment should be discounted until the assessment methodology is finalised.

ACT Position

The ACT supports the Commission staff proposal to retain the 2015 Review assessment methodology.

The ACT considers that assessing mining revenue capacity on a mineral-by-mineral basis is more consistent with the principle of *What States Do* than alternative approaches of aggregating the mining revenue assessment.

Our position is that the mineral-by-mineral approach captures differences in royalty structures between the major minerals effectively and improves the accuracy of equalisation as a consequence. Likewise, the ACT also supports the proposed continued equalisation of Commonwealth Government grants in lieu of royalties under the mining revenue assessment.

In addition, the ACT supports the Commission staff proposal to assess mining revenue capacity on the basis of free-on-board value of mineral production. The ACT considers that this method of assessing each State and Territory's mining revenue capacity reflects *What States Do* in recognising that most States and Territories levy royalties on the basis of value of production. Further, the ACT considers that assessing the value of production at free-on-board most accurately captures the value of mineral production for the purposes of mining royalties. The ACT considers that this method captures the value of minerals to the extractor, which is the party that is responsible for paying royalties.

The ACT further supports the Commission's position to not adjust assessed mining revenues for development policies or compliance efforts.

The ACT notes that differences in development policies and compliance efforts are both policy choices on the part of different State and Territory governments and that State and Territory policies have a relatively minor impact on the prospectability of mineral resources compared to the physical occurrence of minerals in each State and Territory. This is evidenced by the 2017 Fraser Institute Annual Survey of Mining Companies. This survey identifies the interactions of prospectivity and policy to determine the most promising jurisdictions in the world to invest in mining projects or build new mines. These influences on mining investment decisions are summarised into a series of indices; the Policy Perception Index, which captures mining companies' perceptions towards jurisdictional policies that impact the mining industry, the Best Practice Mineral Potential Index, which captures the physical mineral potential or prospectivity of each jurisdiction and the Investment Attractiveness Index, which effectively collates the other two indices into an overall score for mining investment attractiveness in each jurisdiction.

The results of the 2017 Fraser Institute Annual Survey of Mining Companies indicate that each State and Territory's world ranking in the Investment Attractiveness Index is more closely aligned with its Best Practice Mineral Potential Index rank than its Policy Perception Index rank. For example, WA is considered by mining companies to be the fifth most attractive investment location for mining in the world and the jurisdiction with the fourth most potential for mineral development. This is compared to a policy perception rank of only 17th. This pattern is observed across all surveyed States and Territories, with each State and Territory's Investment Attractiveness Index rank consistently being closer to its Best Practice Mineral Potential Index rank than its Policy Perception Index rank (Table D.7).

Table D.7: Investment attractiveness, mineral availability and policy perception world rank of each State and Territory

State/Territory	NSW	VIC	QLD	WA	SA	TAS	NT
Policy Perception Index World Rank	53	52	31	17	26	32	33
Best Practices Mineral Potential Index World Rank	40	77	3	4	12	63	33
Investment Attractiveness Index World Rank	46	71	12	5	14	50	27

Source: 2017 Fraser Institute Annual Survey of Mining Companies

Note: The ACT is not considered in the Fraser Institute Annual Survey of Mining Companies

The ACT further notes that business development costs are currently captured under the services to industry assessment, with total expenditure by States and Territories on business development in 2013-14 of \$3.6 billion, or \$155.44 per capita nationally as per the 2015 Review. Moreover, only a portion of these expenses would be related to the development of the mining industry. In addition to business development costs, the ACT also notes that the cost to States of additional infrastructure in mining regions due to population growth is already captured under the Infrastructure assessment. These factors combined indicate that, even if some mining-specific development costs that are not already being assessed were to be identified, a differential assessment of these costs would likely not result in a material impact on the GST distribution.

In addition, the ACT considers that differences between States and Territories in their compliance efforts would have no impact on the free-on-board value of mineral production.

While a greater compliance effort would increase a State/Territory's actual to assessed revenue ratio, the ACT does not consider there to be a conceptual basis for compliance to have an appreciable second order effect on the value of the tax base.

The ACT considers that the costs to States and Territories of developing their mining industries and thus increasing their mining revenue capacity have a comparatively small impact on mining investment compared with the physical incidence of minerals and are likely too small to have a material impact on the GST distribution. On this basis, the ACT supports the Commission's position to not adjust assessed mining revenues for development policies or compliance efforts.

Regarding the Commission staff proposal to assess a portion of any additional revenue generated through a change in royalty rates on an EPC basis, the ACT considers the proposal is an effective way of addressing concerns with *Policy Neutrality* in the assessment of minerals which have production dominated by one or two States or Territories. The ACT is supportive of the Commission staff proposal, though notes that the proposal should be symmetrical i.e. States and Territories that lose mining royalty revenue from cutting their royalty rates should have an equal portion of their lost revenue assessed on an EPC basis. The ACT considers that symmetrical treatment of increases and decreases in royalty revenue from royalty rate changes would act as a safeguard against incentivising under-taxation of mineral resources.

The ACT also supports the Commission proposal to assess banned minerals on an EPC basis. The ACT acknowledges that assessing revenue capacity for minerals that are subject to bans or moratoriums is challenging to the Commission and notes that the 2015 Review approach of assessing States and Territories that have banned development as having no capacity to generate revenue in relevant minerals is not consistent with the principle of *Policy Neutrality*. Given the practical limitations to assessing banned capacity, the ACT considers an EPC assessment to be the most appropriate option.

OTHER REVENUE

Summary

The Other Revenue assessment comprises revenue from gambling taxes, fees and fines, user charges, contributions by trading enterprises, interest and dividend income and other revenue sources which are not elsewhere classified. All revenue in the Other Revenue assessment is assessed EPC.

The ACT supports the Commission staff position to retain the 2015 Review methodology for Other Revenue in all cases other than user charges. We also note the Commission staff intention to assess gambling taxes differentially and set out a proposal to do so in the Gambling Revenue chapter.

The ACT differs from the Commission's current approach to user charges in that we consider user charges to belong on the expense rather than revenue side of assessments, and should accordingly be presented within each relevant expense assessment. The presentation of user charges as Other Revenue in our view detracts from the transparency and clarity of the assessments.

Context

In the 2015 Review, the Other Revenue assessment comprised revenue from:

- Gambling taxes;
- Fees and fines;
- User charges (such as property titles user charges and public safety user charges) but not those associated with admitted patients, housing and functions usually performed by public trading enterprises;
- Contributions by trading enterprises;
- Interest and dividend income; and
- Other revenue, including other taxes and other income not elsewhere classified.

Revenues in this assessment are assessed EPC. An EPC assessment can be made for one of three reasons:

- States and Territories have the same per capita capacity to raise revenue from that source;
- Either the method or the data are not sufficiently reliable to support an assessment; or
- A differential assessment would not be material.

This assessment contained \$44.35 billion of revenue in 2016-17, making it by far the largest of all the revenue assessments.

Commission Staff Position

The Commission is proposing no change to this assessment, with the possible exception of gambling taxes, where staff are exploring whether a differential assessment can be made.

ACT Position

The ACT's position on gambling taxes is set out in the chapter on Gambling Revenue. Implementation of a differential assessment for this component would reduce Other Revenue by approximately \$5.5 billion.

The ACT also considers a different approach from that proposed by the Commission on user charges is more appropriate. This is set out in the section on user charges below. It would entail the removal of all user charges from assessment as Other Revenue, thus removing \$11 billion of revenue from this assessment.

The ACT supports the current treatment of the other components of revenue in this assessment.

User Charges

Context

The treatment of user charges adopted in the 2015 Review across all assessments comprises three different approaches, depending on the circumstances for the related service:

- A net assessment of user charges. This treatment applies if the drivers of user charges are the same as drivers of use of the related service or if the Commission has data on drivers of net cost;
 - This treatment is implemented by netting the user charges from the expenses of the relevant expense assessment. It is the treatment applied to user charges in the Post-secondary Education, Health, Services to Communities and Transport assessments.
- A gross assessment of user charges. This treatment applies if the drivers of user charges are different from the drivers of use of the related service and when a separate assessment of user charges would be material;
 - This treatment is implemented by undertaking the gross assessment and offsetting it against the relevant expense assessment. It is the treatment applied to user charges in the Housing assessment.
- An EPC assessment of user charges. These user charges are gathered together and assessed in the Other Revenue assessment.

Commission Staff Position

The Commission is proposing to continue the user charge treatments applied in the 2015 Review.

ACT Position

The ACT differs from the Commission's current approach to user charges in that we consider user charges to belong on the expense rather than revenue side of assessments, and should accordingly be presented within each relevant expense category. Assessment and presentation of user charges as Other Revenue in our view detracts from the transparency and clarity of the assessments.

User charges¹² relate to the provision of a specific service, offsetting the cost of that service. If the service did not exist, neither would the user charge.

A user charge is not a form of taxation; it does not rely on legislative powers of coercion. If the charge is not paid, the service is not provided. The user charge is, unlike other forms of revenue which are not hypothecated, by definition assigned to a particular expense.

These characteristics support the position that user charges should not be considered a form of revenue, but instead should be assessed within the expenditure assessment to which each type of charge relates, in effect as a “negative expense”.

Such an approach would markedly increase the transparency of assessments and significantly reduce the very large amount currently assigned to the Other Revenue assessment.

There are three main options for assessment of the user charge revenue within each relevant expenditure assessment:

- Netting off user charge revenue from expenses at the national level before assessment of the expenses
- Assessing the user charges EPC before netting off for each State and Territory.
- Making an assessment of gross expenses and separately assessing the user charges, then deducting the assessed user charges from the assessed gross expenses for each State and Territory to give assessed net expenses.

Analysis of these options needs to distinguish between assessing the user charges as revenue and assessing them as a negative expense. The third option above is in effect a revenue assessment embedded in an expense assessment. The other two options are, by contrast, an implicit assessment of the **expenses** which have been netted off.

The first and second options differ, in that the first option in effect assesses the revenue in the same ratio as the needs, whereas the second option assumes no differential needs for the expenses which have been netted off. This means that:

- The first option in effect assesses the revenue in the same ratio as the expense needs i.e. States and Territories with above average needs will also have above average revenue raising capacity (an implied differential assessment of the revenue).
 - At first glance this appears counter-intuitive, in that States and Territories with higher average needs due to economic disadvantage would be assumed to have a lower capacity to raise revenue from user charges. However, where services are targeted at lower income or disadvantaged people, with user charges not reflecting full cost, higher needs and higher revenue raising capacity will tend to go together.

¹² User charges are defined by the ACT Government as revenues resulting from the sale of goods and services to consumers. User charges include revenue that the reporting ACT Government entity (Directorate) controls, and excludes ACT administered revenue. User charges exclude Controlled Recurrent Payments (Appropriations).

- This tendency would be reinforced where substitutable private services are available which higher income, more advantaged people are more likely to access. Social housing rents are a good example of this phenomenon. Table D.8 provides a simple example of how this option works.

Table D.8: Assessed revenue, Housing revenue component, 2013–14

	NSW	Vic	Qld	WA	SA	Tas	ACT	NT	Total
Total (\$m)	977	726	618	328	255	64	37	42	3,048
Total (\$pc)	131	125	132	129	152	125	96	173	131
Assessed Diff (\$pc)	0	6	-1	2	-21	6	35	-42	0
Assessed Diff (\$m)	0.00	34.72	-4.69	5.10	-35.22	3.08	13.44	-10.25	0.00

Source: 2015 Review Report Vol 2, Commission calculation.

- By contrast, full cost user charging indicates a service which is available to all, without means testing. However, such services normally also provide concessional rates for low income users e.g. concessional public transport fares for pensioners. Such concessions are best treated as an expense under the Welfare assessment, with an equivalent amount added back to revenue to produce a gross assessment of the associated revenue (as applied to stamp duty concessions for first home buyers). Full cost user charging means that States' and Territories' fiscal capacities are not affected by the associated expense, indicating that netting off nationally prior to assessment is the appropriate treatment of such revenue.
- The second option in effect assumes that all States and Territories have the same per capita capacity to raise user charge revenue. This can only be determined on an assessment by assessment basis and is unlikely to apply in most cases. However, it is useful to examine it to distinguish the impact from the netting off of user charges nationally (prior to assessment) – as shown in the illustration below.
- The third option, a separate, differential assessment of user charge revenue, can be based on capacity to pay, where the amount of the charge depends on an individual's income and/or assets. This applies in the example of social housing rents, where rents are capped at 25 per cent of a tenant's gross household income. In such cases, the revenue should be differentially assessed and netted off expenses for each State and Territory.

The above discussion assumes that the relative needs of States and Territories are not affected by the total amount of money spent (i.e. there is no second order effect on the underlying disabilities). This assumption is reasonable in the context of the GST redistribution being aimed at compensating for underlying disabilities rather than reforming or reducing them and on the likelihood that increased State and Territory expenditure due to population growth and inflation will not change real per capita needs.

Table D.8 below shows user charge revenue for each expense category as a percentage of gross expenses in each category, for the assessment years of the 2018 Update, and the assessment treatment applied in each category. User charges represent over 10% of gross expenses in eight expense categories, and over 20% in four categories.

**ACT GOVERNMENT RESPONSE ON COMMONWEALTH GRANTS COMMISSION 2020
REVIEW DRAFT ASSESSMENT PAPERS**

Table D.9 User Charges by Expense Category

Three-Year Averages	Category Expenses	User Charges	User Charges as percentage of Expenses	Assessment Treatment 2015 Review	Commission Proposed Assessment Treatment 2020 Review	ACT proposed assessment Treatment 2020 Review
Health	64,359	7,418	11.53%	Net off nationally	Net off nationally	Net off nationally before assessing
Housing	6,253	3,122	49.93%	Differential	Differential	Net off nationally before assessing
Justice	18,250	1,559	8.54%	Other revenue EPC	Other revenue EPC	Within assessment EPC
Other expenses	30,010	3,534	11.78%	Other revenue EPC	Other revenue EPC	Within assessment EPC
Post-secondary education	6,620	1,647	24.88%	Net off nationally	Net off fee for service	Gross assessed deduction
Roads	6,560	1,982	30.21%	Other revenue EPC	Other revenue EPC	Within assessment EPC
Schools education	50,227	1,198	2.38%	Other revenue EPC	Net off by State	Net off by State
Services to communities	7,907	1,446	18.29%	Varies	Other revenue EPC	Within assessment EPC
Services to industry	7,373	1,560	21.16%	Varies	Net off nationally	Net off nationally before assessing
Transport	15,914	2,808	17.64%	Net off nationally	Net off nationally	Net off nationally before assessing
Welfare	16,529	460	2.78%	Other revenue EPC	Other revenue EPC	Within assessment EPC
Total	230,002	26,734	11.62%			

Source: 2018 Update, ASOL data.

Figure D.2: Impact of netting off user charge revenue versus EPC assessment.

Gross National Expenses \$10b

Total User Charges \$1b

Net National Expenses \$9b

Assume there are only two States, with equal populations. Also assume the States' relative needs compared to EPC are:

State One 1.1

State Two 0.9

Ratio of State One needs to State Two needs = 1.1:0.9 = 1.22222.

Option One – Net off User Charges before Assessment

State One needs $1.1/2.0 = 0.55 \times \$9b = \$4.95b$

State Two needs $0.9/2.0 = 0.45 \times \$9b = \$4.05b$

Ratio of State One net needs to State Two net needs = 4.95:4.05 = 1.22222

Option Two – Assess Gross Expenses then deduct User Charges EPC

State One needs $1.1/2.0 = 0.55 \times \$10b = \$5.5b$ less \$0.5b UC = \$5.0b

State Two needs $0.9/2.0 = 0.45 \times \$10b = \$4.5b$ less \$0.5b UC = \$4.0b

Ratio of State One net needs to State Two net needs = 5.0:4.0 = 1.25

An EPC assessment of user charge revenue will therefore increase the assessed needs of the higher need State and reduce the assessed needs of the lower need State, with a concomitant larger redistribution of GST. This is because the netting off approach implies a distribution of the user charge revenue which aligns with that of the associated expenses i.e. in this example, the implication is that State One receives \$550 million in user charge revenue and State Two receives \$450 million in user charge revenue.

COMMONWEALTH PAYMENTS

Summary

The ACT receives a range of grants from the Commonwealth in addition to the GST in the form of tied and untied payments, namely, SPPs, NPPs, FAGs and MSPs. The HFE process takes into account Commonwealth payments to each State and Territory with some payments being fully or partially equalised, while others are excluded from the process entirely.

The ACT supports the principle that Commonwealth payments which are allocated on a needs basis should be treated as EPC under the HFE process and payments that are distributed on an EPC basis should be assessed differentially. This would avoid one process undoing the other.

The ACT argues that the current equalisation treatment of infrastructure funding, namely the application of a 50 per cent discount to Commonwealth funding for NNROs and NNRA, is one of the most significant areas of weakness in the HFE system as, unlike other assessment categories, it is characterised by fundamental inequities. The fundamental causes of these inequities reflect an uneven distribution of Commonwealth payments to the States and Territories for infrastructure and on the quarantining from equalisation of a major proportion of those payments.

The equalisation process should be used to the fullest extent possible to correct them. This requires both a commitment by the Commonwealth Government to avoid quarantining infrastructure payments from equalisation in other than exceptional circumstances and a commitment by the Commission to review the application of a 50 per cent discount to Commonwealth funding for NNROs and NNRA.

The ACT considers that the Commonwealth Government should address the potential unwinding of penalties through new intergovernmental agreements such as the NHHA and Quality Schools through the HFE process and how the Commission should address this issue.

Context

The ACT receives a range of grants from the Commonwealth in addition to the GST in the form of tied and untied payments, namely, SPPs, NPPs, FAGs and MSPs¹³. Total funding for the ACT from these sources is estimated at \$896 million for 2018-19.

There have been major new developments involving new national agreements and changes to associated SPPs which will impact funding for the ACT from 2018-19 onwards. COAG has overseen the development of new national agreements in areas of national significance, with progress in key policy areas including education and health reform.

¹³ FAGs are paid to State and Territory governments for provision to local governments through the State/Territory Grants Commissions. These payments are untied and can be spent according to local government priorities. MSPs are provided to the ACT to assist in meeting the additional local government municipal costs which arise from Canberra's role as the national capital. These payments and FAGs are excluded from the equalisation process.

In this environment, progress has been made in providing funding certainty in key areas over the course of 2017-18, with the passage of legislation in the Commonwealth Parliament and the negotiation of agreements in relation to education funding, housing and homelessness funding and the signing of a Heads of Agreement for public hospital and health reform funding for five years from 1 July 2020.

Underlying the negotiation of national agreements is how Commonwealth payments are treated through the HFE process. This process takes into account Commonwealth payments to each State and Territory with some payments being fully or partially equalised, while others are excluded from the process all together.

The Commission's conventional process involves a comprehensive analysis of State and Territory expenditure needs in each assessment, based on drivers of expenditure which are not susceptible to influence by State and Territory government policy. Once needs have been assessed for each State and Territory, the Commonwealth payments received by each State and Territory are then deducted from its assessed needs to give a net outcome for GST distribution.

The consequence is that any State or Territory which receives a share of Commonwealth payments greater than its share of national expenditure needs as assessed by the Commission will incur an equal offsetting loss in GST compared with an EPC assessment. Similarly, any State or Territory which receives a share of Commonwealth payments less than its share of national expenditure needs will receive an equal offsetting gain in GST compared with an EPC assessment.

The Commission staff Draft Assessment Papers touch on each Commonwealth payment relevant to that particular assessment. This section of the ACT submission focuses on the principles that govern the treatment of Commonwealth payments through the equalisation process.

Commission Staff Position

As outlined in the 2015 Review, if Commonwealth payments can be used to offset the fiscal impact of innate differences, then only the residual fiscal consequences should impact on the GST distribution. In this way, Commonwealth payments affect the GST distribution. If Commonwealth payments were not included in the equalisation process, some States and Territories would have the capacity to deliver above average services and the Commission's objective of achieving HFE would not be achieved.

As a result, the Commission adopted the guideline in the 2015 Review that payments which support State and Territory services and for which expenditure needs are assessed will impact the relativities. While this is not necessarily the guideline on the treatment of Commonwealth payments by the Commission as presented in the IGA-FFR, which posits that National Partnership facilitation and reward payments should be excluded from equalisation while GRA payments, SPPs, NHRA funding and National Partnership project payments should be included, the Commission has consistently been given significant discretion over its treatment of Commonwealth payments in the HFE process. Commonwealth payments are examined on a case-by-case basis by the Commission.

Following this guideline, the Commission's decision to include or exclude a Commonwealth payment from the equalisation process is made purely on the basis of whether the payment is available to support State and Territory services and whether needs have been assessed.

Needs Based Funding Models

Context

The Commonwealth provides grants to the States and Territories in the form of SPPs to support services in health, education, skills and workforce development and housing.

Major reforms in recent years to health and education have significantly changed the distribution of funding under these agreements. The NHRA and NERA moved the basis of funding allocation to the States and Territories from EPC to an individual needs basis. The individual needs basis of allocation is represented by the ABF method in health and the SRS in education.

In relation to health, the Commonwealth and the States and Territories signed an agreement in April 2016 to extend the current funding arrangements, including ABF and the NEP, for three years to June 2020.

- The allocation of funding to the States and Territories under the ABF model is determined by the actual number of hospital-based services delivered by each State and Territory, weighted according to the resource impact of each type of service. The weighted number of services is multiplied by the NEP, which is set by the IHPA.
- The NEP includes loadings (adjustments) which are designed to take account of legitimate and unavoidable variations in the costs of delivering health care services, including remoteness, indigeneity, private contributions and patient complexity.

In relation to Education, the Commonwealth Government has maintained the current SRS-based funding to the end of 2017 and introduced a revised version of this model (Quality Schools) which commenced from the start of the 2018 school year.

- Allocation of funding to the States and Territories under the SRS model is determined by the actual number of students enrolled at each public school, with student-based loadings for disability, indigeneity, SES and low English proficiency, as well as school-based loadings for school location and school size.
- Per student funding for non-government schools is also adjusted according to each school's capacity to contribute, which takes into account parents' ability to contribute, based on the average SES of their residential area, and other sources of private income.

The other main sectors of Commonwealth SPP funding to the States and Territories are disability services, skills and workforce development and housing.

- Following the 2008 IGA-FFR, these three SPPs progressively transitioned to an EPC allocation over a five-year period, ending in July 2014. While the skills and housing SPPs continue to be allocated on an EPC basis, the disability SPP is now being phased out during the transition to the NDIS.
- NDIS represents a different model again, with EPC contributions from the States and Territories, which are in the nature of insurance premiums for all their citizens and allocation of funds to individual participants on a needs basis.

Needs-based funding models delivered through SPPs determine needs of broad population groups which are considered to differ significantly in the amount of funding per person required to deliver an equivalent outcome. This is very similar to the HFE assessment process, and in both cases leads to an aggregation and allocation of funding at the State/Territory level. In principle, there is significant potential for overlap or conflict.

NDIS differs significantly in that needs are determined for each individual, in accordance with a set of criteria, and funding is allocated to the individual as a “package”. As a national scheme with State and Territory contributions on an EPC basis, NDIS has removed the need for Commission involvement via HFE. Once Full Scheme NDIS is in place, there will be no equalisation required for the disability sector (except to the extent that some residual State and Territory funded services may remain).

However, funding in other sectors does not and is not likely to operate under a national contributory scheme, so equalisation will continue to apply for the foreseeable future.

ACT Position

A range of different models have been applied to the interaction of needs-based funding and HFE in the main sectors of Commonwealth funding, with no particular logic to explain why the different approaches have been adopted.

- The skills/housing model represents one end of a spectrum, giving the whole task of needs-based assessment to the Commission.
- The education and health models represent two variants in the middle of the spectrum, with hybrid approaches combining needs-based elements in the Commonwealth funding arrangements, with complementary needs-based elements in the Commission’s assessments.
- NDIS could be considered as representing the other end of the spectrum, where the Commonwealth funding model reflects all relevant needs and there is no redistributive role for the Commission.

An alternative approach would be to apply a comprehensive needs-based approach to the allocation of all Commonwealth funding and then quarantine expenditure of this funding, through ToR to the Commission, from redistribution or unwinding via the HFE process. Commission advice could still be drawn on in the development of the parameters of such funding models. This approach would also avoid duplication and unwinding in relation to the Commonwealth funding allocation, though there is the issue of whether it is desirable for expenditure funded by State and Territory own-revenue to then be assessed by the Commission on a different needs basis from the assessment of the Commonwealth-funded expenditure.

In the future development of new, or revision of existing, Commonwealth funding models in major sectors of State and Territory service delivery it would be appropriate to deliberately consider for each model whether a needs-based allocation of funding should be the objective and, if so, how the role of the Commission and the HFE process fits into that. Commonwealth Treasury should as a matter of course seek the advice of the Commission early in the development of such models.

The ACT supports the principle whereby Commonwealth payments that are allocated on a needs basis should be treated as EPC under the HFE process and payments that are distributed on an EPC basis should be assessed differentially. This would avoid one process undoing the other.

Full or Partial Exclusion of Commonwealth Payments

Context

In the 2015 Review, the Commission treated only half of Commonwealth payments to States for NNROs and NNRA as having an impact on the GST distribution. The basis of this decision was that the Commission considered the Roads assessment did not fully capture the underlying drivers of construction expenditure on NNROs. The Commission argued expenditure on NNROs was partly driven by Commonwealth decisions that were not reflected in the Roads assessment, notably to support national economic growth and efficiency.

However, many States disagreed with this approach on the basis that the Commission's Roads assessment adequately captured the drivers of investment on NNROs and that States and Territories have some influence on Commonwealth decisions on which roads are classified as NNROs.

Commission staff are seeking State and Territory views on whether the Commission should continue to discount 50 per cent (or another proportion) of Commonwealth payments to States and Territories for NNROs and NNRA or if these grants should have no impact on the GST distribution.

ACT Position

The ACT contends the current equalisation treatment of infrastructure funding is one of the most significant areas of weakness in the system as, unlike other assessment categories, it is characterised by fundamental inequities.

The key causes of these inequities reflect an uneven distribution of Commonwealth payments to the States and Territories for infrastructure and on the quarantining from equalisation of a major proportion of those payments.

As noted by the Grattan Institute in their submission to the PC inquiry into HFE, quarantining of spending on NNROs and NNRA is only justifiable if it is limited to nationally important roads and railway lines. However, given the strong incentives for stakeholders to lobby the Commonwealth, expenditure on NNRO and NNRA infrastructure is likely, at least in part, driven by political gain rather than the national interest.

- The Grattan Institute argue the Commonwealth has historically consistently spent more on transport infrastructure in NSW and QLD compared to other States and Territories, including for NNRO and NNRA projects.
 - The significance of these States is that recent federal elections were heavily influenced by the number of NSW and QLD seats that changed hands. In the past seven federal elections, one of the major parties gained an average of five seats from the other in each of NSW and QLD.
 - This is compared to VIC, which has, on average, contributed only one seat to the swing in the past seven elections.

- The Grattan Institute also argue the current approach to quarantining some payments and not others creates a complex system where decision makers are not always fully aware of the impact of their decisions on State and Territory budgets.
- The Grattan Institute highlighted these issues by querying the justification for the NNRO status of the Geelong–Coolac road. It argued that while Geelong is an important centre of commercial activity, Colac does not qualify as a transport hub or commercial centre and use by freight vehicles on this section of road is much lower than most other NNROs. As a result, the Grattan Institute did not consider it a project of national significance.

Current year and budgeted Commonwealth infrastructure spending over the next four years shows enormous variability of per capita funding across the States and Territories, with the NT and QLD receiving amounts around four to five times the payments received by the ACT and VIC. In the context of relativities or category factors assessed by the Commission, this represents a range of 0.487 (VIC) to 2.421 (NT). The Infrastructure assessment in the 2018 Update had a different range of 0.419 to 1.264, indicating the assessment of the relative needs of each State and Territory differed significantly from the Commonwealth Budget allocations. It would be very difficult to argue that the Commonwealth Budget distribution of funding is in any way reflective of need. As a result, Commonwealth infrastructure spending will have a significant impact on a State/Territory's ability to provide services, and if not included in the equalisation process, would give the favoured States and Territories a fiscal advantage over those not so favoured.

The equalisation process should be used to the fullest extent possible to correct these inequities. This requires both a commitment by the Commonwealth Government to avoid quarantining infrastructure payments from equalisation in other than exceptional circumstances and a commitment by the Commission to review the application of a 50 per cent discount to Commonwealth funding for NNROs and NNRA.

An analysis undertaken by ACT Treasury in October 2014 showed an average exclusion of 50 per cent of total Commonwealth infrastructure payments from equalisation over the period 2013-14 to 2017-18.

The ACT understands that ToR are commonly used by the Commonwealth Treasurer to prevent equalisation of grants for specific projects which the Commonwealth Government considers are achieving some desirable objective which they do not wish to see unwound by the Commission process. A good example of this is the decision to quarantine the Asset Recycling Initiative from equalisation, which all governments agreed to from the outset.

The exclusion of 50 per cent of NNRO and NNRA funding from equalisation is based on an estimate of assumed benefits to other States and Territories and the Commonwealth, but the 50 per cent is an arbitrary figure applied by the Commission to all such projects, with no attempt made to quantify the actual distribution of benefits across jurisdictions.

In the absence of a measurable distribution of benefits, the ACT recommends the discount on Commonwealth payments for national infrastructure projects should be discontinued other than in exceptional circumstances, which should be outlined in the ToR.

Treatment of Financial Penalties

Context

The approach recently taken by the Commonwealth to influence the outcome of national agreements is to include provisions for financial penalties for States and Territories which do not meet agreed outcomes or objectives. This approach has been used with the new Quality Schools program and the NHHA, which represents a major departure from the Commonwealth's previous policies in federal financial relations in relation to SPPs.

The inclusion of financial penalty provisions in these new agreements presents a challenge for the Commission in how they should be treated for equalisation purposes. Use of entitlements (payments before application of penalties) would prevent the assessment unwinding any penalties imposed by the Commonwealth under the new agreements. On the other hand, use of actuals (payments after application of penalties) would unwind the penalties because the affected States and Territories would receive a compensating increase in their GST payment.

Application by the Commission of the conventional backcasting arrangement to these SPPs would necessitate following the entitlement approach, as penalties cannot be forecast. However, application of assessment year distributions would enable the Commission to use the actuals approach, if it considered that more appropriate.

Commission Staff Position

The Commission considered this issue in relation to the Quality Schools program as part of the 2018 Update. In the Update Report it decided to cease backcasting because of uncertainty about the distribution of application year funds. However, no penalties had been applied during the assessment years of this Update, so the distribution could only be done on the basis of State and Territory entitlements. A decision on the treatment of any penalties beyond this period was left to subsequent Updates.

In relation to the NHHA, where penalties also apply if objectives are not met, the Commission decided not to backcast payments because they did not consider that the new agreement involved a major change in federal financial arrangements. This view was based on the fact that there was no significant change in the quantum or distribution of payments under the new agreement. The Commission also considered that it did not have enough information at that time to decide how to treat financial penalties. This was also deferred to a future Update, given that penalties could not come into effect before the 2018-19 assessment year.

ACT Position

The ACT acknowledges that backcasting can only occur where application year entitlements by State and Territory are known with certainty in advance. If there is uncertainty, then assessment year distributions must be used. The latter scenario enables the Commission to apply either an entitlement or actual approach to the assessment of the Commonwealth payments.

Although the Commission would normally assess the payments actually received, this would have the effect of unwinding any penalties. It would be well within the rights of the Commonwealth to specify, through ToR, that the Commission assess the payments so as to prevent such unwinding, i.e. to base them on entitlements instead.

ACT GOVERNMENT RESPONSE ON COMMONWEALTH GRANTS COMMISSION 2020 REVIEW DRAFT ASSESSMENT PAPERS

In its submission on the 2018 Update New Issues Paper, the ACT contended that, although the new NHHA did not involve a significant change to the quantum or distribution of payments, it should be regarded as embodying a major change in federal financial relations arrangements, for three reasons:

- It converted the previous Homelessness NPP funding into ongoing SPP funding.
- Its provisions were incorporated in Commonwealth legislation, rather than depending solely on inter-governmental agreements.
- It contained provisions for financial penalties where certain performance requirements were not met.

The ACT continues to hold this view, of which the second and third dot points above apply also to the Quality Schools program.

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EXPENSE ASSESSMENTS

SCHOOLS EDUCATION

Summary

The Commission assesses State and Territory expenditure on government and non-government schools in the Schools Education assessment. It also takes into account the funding that the Commonwealth Government provides for both government and non-government schools.

- Commission staff are still deliberating on the regression model to be used to determine per student funding provided by each State and Territory.
 - The ACT supports the broad approach suggested by Commission staff. We also agree that ICSEA should be used to measure SES.
- The ACT is supportive of the Commission staff proposal to offset user charges from State and Territory expenses in the Schools Education assessment as we contend it improves transparency of the assessment.
- We support the Commission staff proposal to continue the 2015 Review method of using the Commonwealth's SRS to assess the need for Commonwealth funded government schools.
- The ACT is supportive of the Commission staff recommendation to treat Commonwealth funding for non-government schools in the same way as other Commonwealth payments that do not affect State and Territory shares of GST revenue.
- The ACT supports the Commission staff recommendation to continue the 2015 Review practice of using ABS data, with the geographic distribution being based on ACARA data, for student numbers.
- We support the Commission staff recommendation not to incorporate students with a disability into the Schools Education assessment unless it is clear these data are comparable across States and Territories.
- We support the Commission staff recommendation to use the actual number of government and non-government students in each State and Territory as a policy neutral measure of the number of students.
- The ACT does not concur with the Commission staff proposal on the assessment of student transport expenses. Among the three options for assessing school transport expenses that the Commission staff propose, the ACT supports the proposal to assess school transport expenses in the Other Expenses assessment, with no differential assessment of such expenses.

Context

The Schools Education assessment covers State and Territory and Commonwealth spending on both government and non-government schools, including preschool education and student transport. Commonwealth funding covers a certain proportion of the cost States and Territories would have otherwise incurred on government and non-government schools.

In the 2015 Review, the Schools Education assessment assessed State and Territory funding for schools, Commonwealth funding for government and non-government schools and student transport funding using different methods. Depreciation and investment in Schools Education were assessed in the Depreciation and Investment assessments, based only on government school enrolments.

School expenses funded by States and Territories were assessed using the actual number of students in each State and Territory, with adjustments for the higher costs of indigenous students, socio-economically disadvantaged students, students in remote schools and schools in small isolated communities. The assessment also took into account the higher costs to States and Territories of students in government schools relative to students in non-government schools.

These adjustments were calculated through a regression of ACARA data, with the regression establishing the relationship between State and Territory government funding of a school and its student profile. Separate regressions were used for government and non-government schools. An adjustment for wages was also made to take into account that wage costs were higher in some States and Territories than others.

Government school expenses funded by the Commonwealth were assessed such that the educational disadvantages embedded in the NERA were not unwound by the GST distribution process. Hence, until the 2017 Update the assessment was based on projected application year enrolment data with cost loadings for different types of students from the SRS for government students. A small change was made in the 2018 Update with the assessment now being based on assessment year enrolment data and not application year enrolment data.

As far as non-government school expenses funded by the Commonwealth were concerned, since those funds did not have any impact on State and Territory fiscal capacities, they had no impact on the GST distribution. Both the payment and the associated expenses were assessed on the basis of actuals, thereby cancelling each other out.

Student transport was assessed using actual student numbers, with different weights for urban and rural students. A further adjustment was also made to take into account the distance rural students needed to commute to attend school.

Finally, as mentioned above, depreciation and investment in Schools Education were assessed in those respective categories, based on the enrolments in government schools. Only indigenous students in schools with at least 25 per cent enrolments originating from them attracted a cost weight. Since small schools require more capital and need to incur more recurrent expenditure per student, the SDS disability was also applied to depreciation and investment. Additionally, since growth in enrolments also drives assessed investment need, population growth and changing disabilities were used as indirect measures of investment needs.

The Schools Education assessment redistributed \$80 million, or \$190 per capita in GST revenue from the ACT in the 2018 Update.

Specification of the Regression Model

Context

In the 2015 Review, the Commission used a relatively complex regression model where it had to split the cost of supporting indigenous and non-indigenous students at the school level, according to the number of such students enrolled, with funding per student assumed to be equal for each group of students. Thus, each school had two records. Such a relatively complex approach could partly be attributed to the fact that the simpler model with a single record for each school produced results which were non-intuitive and lacked a conceptual basis, e.g. regression results using the simpler model showed that indigenous students in more disadvantaged areas received less funding than indigenous students in less disadvantaged areas.

In the 2020 Review, Commission staff are attempting to develop an assessment in three stages:

- Developing a model that explains differences in State and Territory expenditure between schools which allows for different students within the same school to be allocated different levels of resourcing;
- Incorporating additional data from the Commonwealth Government Department of Education and Training; and
- Working with State and Territory funding formulas and other sources to refine the model so that the variables included in the model reflect a strong conceptual case for their inclusion and are sufficiently policy neutral.

Commission staff analysis has shown that:

- While school type (primary/secondary/combined) is a strong predictor of school costs, it is inappropriate to use for the allocation of GST as it significantly reflects State and Territory policy choice. This is on the ground that major differences between States and Territories in the proportions of primary and secondary students are driven by SA's policy decision to include Year Seven in primary school.
- Similarly, while school size is an important factor in determining school education expenses, it is also significantly impacted by State and Territory policy choice since States and Territories can choose to have a few large schools or many small schools. However, school size becomes a factor in areas where the SDS disability is applicable as schools in such areas tend to have, on an average, more students than other areas. Thus Commission staff incorporate school size in the regression model only through the SDS disability.
- Inclusion of attendance, along with enrolments, significantly improves the model.

- There is a strong conceptual case that students from low SES backgrounds attract more State and Territory funding than students from high SES backgrounds. However, Commission staff are yet to finalise the approach to measure SES using the data available – whether to use IRSEO/NISEIFA for indigenous/non-indigenous students or to use the ICSEA value that is allocated to a student based on the attributes of the student, parents and the area of residence.

Commission Staff Position

Staff propose to recommend the Commission use an appropriate regression model reflecting State and Territory funding models once further developed following consultation between staff and the States and Territories.

ACT Position

The ACT supports the Commission staff position that further work on the regression model be carried out, particularly with regard to the following aspects:

- Given the Commission staff view that, in the areas where the SDS disability is applicable, schools have **more** students (as opposed to less), it is not clear whether the SDS disability should be applicable at all. The SDS disability is applied where there are diseconomies of scale leading to a higher per student cost. In this case, considering that there are 'more' students, it is indicative of economies of scale, which would lead to a lower per student cost.
- The regression results incorporating the variables on **school attendance** and **students enrolled but not attending** lack a conceptual basis and do not provide a convincing argument for the addition of such variables.
 - Expenditure on an enrolled but not attending student is highly likely to be dependent on individual school policy and not an intrinsic characteristic of either students or schools. Further, the ACT questions whether school attendance data is reliable. We ask the Commission staff to examine whether attendance at the school level is stable over time. At this stage, the ACT's view is that inclusion of variables such as attendance and students enrolled but not attending would not contribute to improving the quality of the assessment.
 - It is difficult to understand why a State or Territory would spend \$16,100 on an absent non-indigenous student, which is almost as much as an attending indigenous student (\$17,400) and almost three times the expenditure on an attending non-indigenous student (\$5,600).
 - Also, it is worth noting that the expenditure for an absent non-indigenous student (\$16,100) is greater than the expenditure for an absent indigenous student (\$13,700), which is also counter-intuitive since the expenditure on an attending indigenous student (\$17,400) is more than three times the expense on an attending non-indigenous student (\$5,600).
 - Our Education Directorate has also stated that school attendance has never been identified as a significant cost driver for the ACT's schools.

- While using IRSEO/NISEIFA would enable the Commission to differentiate between funding for indigenous and non-indigenous students, it would not enable the Commission to develop a model “which allows for different students within the same school to be allocated different levels of resourcing” (CGC 2018-01/10-S, p. 5, para 22). Hence the ACT supports the use of ICSEA for capturing students’ SES.
 - Using IRSEO/NISEIFA, all indigenous/non-indigenous students in a school are allotted the same SES score, since the scores depend on the location of the school. As the individual student’s SES is **not** taken into account, two indigenous or non-indigenous students from different SES backgrounds will have the same score (though the SES score is likely to differ between indigenous and non-indigenous students). This does not enable the Commission staff to build a model “which allows for different students within the same school to be allocated different levels of resourcing”.
- The fact that ICSEA enables each student’s SES background to be taken into account indicates that ICSEA would be a better measure to use in order to support the conceptual case that Commission staff have proposed.
- According to our Education Directorate, ICSEA already incorporates remoteness as a factor. Thus, if ICSEA is used to measure SES, the variables used in the regression model to capture remoteness may have to be dropped or modified accordingly.

User Charges

Context

According to GFS figures, States and Territories raised \$1.1 billion from user charges in school education, with the figure as a percentage of government funding varying from one per cent in NSW to six per cent in SA. In 2015, revenue from user charges was assessed EPC in the Other Revenue assessment. Commission staff consider it would be better assessed by netting off against expenses incurred in the State and Territory funding of government schools, which the ACARA dataset enables.

Commission Staff Position

Staff propose to recommend the Commission net user charges off the State and Territory funded government school assessment.

ACT Position

The ACT supports the staff proposal. The ACT has consistently argued for assessing user charges in the individual expense assessments since we consider that it makes the assessment more transparent. We note that the ACARA data on State and Territory expenses is net of user charges, which also is in line with the Commission staff proposal.

Commonwealth Funding of Government Schools

Context

In the 2015 Review the Commission’s ToR instructed that educational disadvantages embedded in the NERA should not be unwound by the GST distribution process.

Hence, Commission staff consider that the Commission has two options namely, continuing the assessment as it currently does or specifying the ACARA data regression to include both Commonwealth and State and Territory funding for government schools.

Commission Staff Position

Staff propose to recommend the Commission use the Commonwealth's SRS to assess need for government school expenses funded by the Commonwealth Government.

ACT Position

The ACT supports the Commission staff recommendation since Commonwealth funding of government schools is determined on the basis of the Commonwealth's SRS and is not influenced by State and Territory policy/funding models.

Commonwealth Funding of Non-government Schools

Context

In the 2015 Review, Commonwealth payments for non-government schools were assessed both as a revenue and an expense, thereby offsetting each other.

Commission Staff Position

Staff propose to recommend the Commission assess Commonwealth funding to non-government schools in the same way as for other Commonwealth payments that do not affect State and Territory shares of GST revenue.

ACT Position

The ACT supports the Commission staff position.

Data Source for Student Numbers

Context

There are two different sources for student numbers – ABS' Schools Australia and data published on the My Schools website by ACARA. The latter is a richer dataset, including data on geography, SES (IRSEO/NISEIFA) and attendance rates. However, it is not published as frequently as the ABS data. Thus, Commission staff use student attribute shares from ACARA data to allocate student numbers available in ABS data (in the 2018 Update, staff used 2015 ACARA data and 2016 ABS data).

Commission Staff Position

Staff propose to recommend the Commission continue the 2015 Review practice of using ABS data with splits of geographic distribution based on ACARA data.

ACT Position

The ACT supports the Commission staff recommendation.

Students with Disabilities

Context

The Quality Schools funding formula indicates that students with a disability cost about three times as much as students without a disability. It is known that States and Territories provide additional resources to students with disabilities.

If their funding is also around the level of the Commonwealth, in combination with the fact that the proportion of students with disability vary from a low of about 2.8 per cent in WA to a high of about 8.2 per cent in the NT (2016 figures), an assessment of students with disability could be material.

The States and Territories and the Commonwealth have recently developed the NCCD. However, according to an ABC News article cited in the Draft Assessment Paper, the Commonwealth Education Minister is quoted that the NCCD has not reached “a credible landing point just yet”. Commission staff contend that it is unlikely the data will be proven to be reliable in time for the 2020 Review.

Commission Staff Position

Staff propose to recommend the Commission not incorporate students with a disability into the Schools education assessment unless it is clear these data are comparable across States and Territories (i.e. definitions of disability are consistent across jurisdictions).

ACT Position

The ACT supports the Commission staff recommendation. Our Education Directorate agrees that the NCCD is yet to deliver nationally consistent and reliable data on the number of students with disability in each category of adjustment.

Policy Effects on State and Territory Shares of Government and Non-government Students

Context

Commission staff argue that there are significant demographic drivers (i.e. non-State/Territory policy impacted) of school choice, noting that students from specific religious groups, from higher income families and from less remote areas are more likely to attend non-government schools. At the same time, Commission staff have investigated whether the proportions of students in non-government schools are also due to the impact of some State and Territory government policies, e.g. the level of funding support and the quality of the government school system.

As a result of their investigation, Commission staff have concluded that the difference between the actual and expected enrolment patterns (the latter dependent on the religious, income and remoteness mix of the students in a State or Territory) can largely be considered to reflect circumstances beyond the control of a State or Territory. For example, in a city with high housing costs such as Sydney, the increase in disposable income that comes from a higher income is not as great as in a low housing cost city like Adelaide. Commission staff argue this potentially explains why the increase in non-government school attendance with increasing income is much less in Sydney than in Adelaide.

Hence, Commission staff propose to use the actual proportion of students in non-government schools in each State and Territory as the best policy neutral measure of the proportion of students in non-government schools in each State and Territory.

Commission Staff Position

Staff propose to recommend the Commission use the actual numbers of government and non-government students in each State and Territory.

ACT Position

The ACT supports the Commission staff recommendation.

Student Transport

Context

Commission staff argue that the current assessment of student transport is based on poor quality data as some States and Territories have difficulty in separating the costs of transport of school students from the cost of transport of other people. Also, the assessment is quite complex and is not material, redistributing just \$27 per capita to the NT.

Hence, Commission staff argue that student transport should not be separately assessed and suggest three options for the assessment of such expenses:

- Include them in Other Expenses and not assess them differentially;
- Group them with school expenses and assess them using the State and Territory funded school education disabilities; or
- Group them with transport expenses and assess them using the urban transport assessment.

Commission staff consider that the disabilities affecting the cost of transporting school children are likely to be more closely related to the disabilities affecting the cost of transporting other people, than to the disabilities affecting the cost of educating school children.

Commission Staff Position

Staff propose to recommend the Commission include transport of school children expenses with transport expenses and assess this using the same the disabilities as those for the urban transport assessment.

ACT Position

The ACT does not support the Commission staff recommendation. We consider that the cost of student transport is primarily driven by the high cost of transport for rural students on a per capita basis. Hence, assessing them using the same disabilities as those for the urban transport assessment would not be conceptually accurate since city size/population is considered as the major driver of recurrent urban transport expenses. The ACT recommends that student transport is retained in the Schools Education assessment but assessed EPC.

POST-SECONDARY EDUCATION

Summary

The Post-secondary Education assessment captures the cost to the States and Territories of providing higher education to their citizens. This is largely restricted to VET rather than funding for universities, which only receive approximately five per cent of States' and Territories' Post-secondary Education funding.

The ACT supports the Commission staff proposal to implement a specific regional cost loading for the Post-secondary Education assessment. The proposed approach is, in the ACT's view, more consistent with the principle of *What States Do* and would be more accurate in achieving HFE. We also support the Commission proposal to retain the indigenous cost loading and update it to reflect more recent State and Territory data. The ACT considers that updating the indigenous cost loading would increase the accuracy of the loading and would also be consistent with the principle of *Contemporaneity*.

The ACT further supports the Commission staff proposal to investigate a possible cost loading for qualification levels, though we recommend that separate cost loadings be applied for trade and non-trade qualifications.

We also support the Commission staff proposal not to investigate a possible cost loading for education provider sector. The ACT agrees with Commission staff that the mix of private and public providers is too heavily influenced by State and Territory policy for a cost loading to be feasible and consistent with the principle of *Policy Neutrality*.

The ACT also agrees with the Commission staff proposal not to investigate a cost loading for course mix, on the basis that both the courses provided and student attendance in courses are strongly influenced by State and Territory policy choice.

The ACT further agrees with the Commission staff proposal to only net fee-for-service user charge revenue against post-secondary education expenses, as there is no conceptual basis for netting off subsidised user charges from Post-secondary Education expenditure.

Context

The Post-secondary Education assessment captures the cost to States and Territories of providing higher education to their citizens. This is largely restricted to VET rather than funding for universities, which only receive approximately five per cent of States' and Territories' Post-secondary Education funding.

Individuals' usage of Post-secondary Education services is associated with certain SDC elements, such as age and SES. Additionally, providing Post-secondary Education services to indigenous and remote communities is generally more expensive to States and Territories than providing services to non-indigenous and urban communities. Consequently, States and Territories which have larger numbers of people as a percentage of their populations which fit the SDC of Post-secondary Education users and who are indigenous and/or reside in remote locations have a greater expense need than States and Territories which have lower population proportions.

In the 2018 Update, the post-secondary education assessment redistributed \$6 million, or \$15 per capita of GST funding to the ACT.

Commission Staff Position

Commission staff, in Draft Assessment Paper 2018-01/11-S, broadly propose to retain the 2015 Review methodology for assessing post-secondary education expenses, with some adjustments to how it assesses regional cost loadings and user charges.

Commission staff propose to retain the regional cost loading, but implement a loading specific to the post-secondary education assessment based on State and Territory funding models. This contrasts with the 2015 Review approach of using the general regional costs gradient in assessing regional cost loading. Further, Commission staff propose to adjust State and Territory data so that only fee-for-service user charges are netted against post-secondary expenses. This contrasts to the 2015 Review methodology of netting all post-secondary education user charge revenue (fee-for-service charges and revenue from other user charges, including subsidised students) against expenses. At a national level, fee-for-service charges comprise 68.7 per cent of all user-charges revenue.

Commission staff propose not to pursue a disability based on whether expenditure on Post-secondary Education is provided to public or private training providers, on the basis that most States and Territories provide the same subsidy to all providers regardless of whether they are public or private institutions and in any case that the mix of public and private providers is highly policy influenced.

Commission staff also propose not to implement a disability for course mix, or for the vocations in which qualifications are being provided, as they consider that States and Territories are unlikely to be able to provide the necessary data and there is significant potential for policy influence in the course mix.

Commission staff further propose to retain the indigenous cost loading and update the loading with recent State and Territory data. Commission staff also propose an investigation into a possible cost loading for qualification levels.

ACT Position

The ACT supports the Commission staff proposal to implement a specific regional cost loading for the Post-secondary Education assessment. The ACT notes that this approach would result in remote and very remote areas gaining considerably more additional assessed expenditure requirements than inner and outer regional areas. The ACT further notes that major cities do not receive any additional loading in either approach.

The ACT notes that most States and Territories do not provide a significant proportion of their training hours in remote and regional areas, with the NT being a key exception. Thus, despite the additional loadings, this proposed change does not have a particularly large impact on the overall GST distribution, with Commission staff estimating that only TAS and the NT would experience changes in their GST distributions above \$10 per capita.

In addition to the minor impact of the change, the ACT considers that using actual State and Territory funding models as the basis for determining cost loadings for Post-secondary Education is more consistent with the principle of *What States Do* than using the general regional cost gradient. Thus, the proposed approach would, in the ACT's view, be more accurate in achieving HFE.

The ACT also notes that the general gradient was only used in the Post-secondary Education assessment due to a lack of data from which to construct a specific regional cost loading. This issue is addressed in the proposed approach.

The ACT also supports the Commission staff proposal to retain the indigenous cost loading and update it to reflect more recent State and Territory data. The ACT recognises that indigeneity results in greater costs in service provision, including for Post-secondary Education and agrees that these additional costs should be recognised in the HFE process. The ACT considers that updating the indigenous cost loading would increase the accuracy of the loading and would also be consistent with the principle of *Contemporaneity*.

The ACT further supports the Commission staff proposal to investigate a possible cost loading for qualification levels. However, we note that there are significant cost differentials between trade (e.g. carpentry, jewellery, etc.) and non-trade (e.g. business administration, ICT, etc.) qualifications at an equivalent level, with trade qualifications costing significantly more in subsidy than non-trade qualifications.

Due to this imbalance, a loading for qualification level that does not take into account the difference in cost between trade and non-trade qualifications could overestimate the additional cost of providing non-trade qualifications and underestimate the additional cost of providing trade qualifications. Given this, the ACT considers that separate cost loadings for qualification level for trade and non-trade qualifications should be explored. We note that the ANZSCO classifications present in the NCVER data would allow the Commission to differentiate between trade and non-trade qualifications for this purpose.

The ACT supports the Commission staff proposal not to investigate a possible cost loading for course mix. While States and Territories may be able to provide data on their expenditure on difference course industries, the ACT notes that State and Territory subsidy policies have a significant influence on the mix of courses and their industries that are provided by both public and private providers, as well as student attendance in these courses. As such, we consider that identifying a cost driver that is consistent with the principle of *Policy Neutrality* would be difficult.

The ACT supports the Commission staff proposal not to investigate a possible cost loading for education provider sector. The ACT agrees with the Commission staff position that the mix of private and public sector post-secondary education service providers is strongly influenced by State and Territory policy. This is evidenced by the experience of VIC from 2008 to 2012.

VIC began to reform its VET sector from 2008, by implementing an uncapped entitlement for all working-age Victorians to train for one subsidised Certificate III at the training provider of their choice. By 2012, all VET subsidies in VIC were fully contestable; able to be used by students of either private or public training providers. Further, VIC reforms also reduced the difficulty in new providers entering the sector, deregulated fees and reduced the per-student subsidy to public institutes to be more comparable with those provided to private providers.

These changes led to significant increases in enrolments in private providers. According to research by the Melbourne Institute of Applied Economic and Social Research for the NCVER in 2014, between 2008 and 2010, private provider enrolments in VIC increased by 60 per cent. Whereas from 2008 to 2011, the growth rate was 300 per cent.

Further, growth in the number of private providers also increased from 36 percent from 2008 to 2010 to 48 per cent from 2008 to 2011.

The VIC growth rates are net of the growth rates experienced by NSW over the same time periods, providing clear indication that the mix of public and private post-secondary education providers in VIC was heavily influenced by the post-secondary education policies of the Victorian Government.

The ACT notes that the study is not without points of contention, given the change in the scope of the NCVET's Government Funded Students and Courses data collection in 2014, which resulted in data being collected on the basis of total VET activity, regardless of whether services were government subsidised or privately funded. This in turn means that the study would not be able to identify actual increases in enrolments in private VET providers. However, the identified shift between private and government subsidised enrolments shows that States and Territories have a significant policy influence over the mix of private and public sector Post-secondary Education providers operating in their jurisdictions. For this reason, the ACT supports the Commission staff in not investigating a possible cost loading for education provider sector.

The ACT further agrees with the Commission staff proposal to only net fee-for-service user charge revenue against post-secondary education expenses. The ACT considers that, as suggested by Commission staff, States and Territories with greater Post-secondary Education expense needs due to their SDC also have a lower capacity to cost recover through user charges on students, as more disadvantaged students would be eligible for more concessions on user charges. That is to say the drivers for Post-secondary Education expenditure needs and subsidised student user charge revenue capacity are inversely correlated.

On this basis, the ACT agrees with the Commission staff position that there is no conceptual basis for netting off subsidised user charges from post-secondary expenditure and supports the proposal to only net off fee-for-service user charge revenue.

HEALTH

Summary

The Health assessment captures the expenditure of the States and Territory on the provision of healthcare services, including hospitals.

The ACT is broadly supportive of the Commission staff proposals for the Health assessment, including those regarding SDC, remoteness and SDS, non-hospital patient transport and CALD.

In particular, the ACT supports the Commission staff position on substitutability, an issue which we have addressed in detail in the attached response to the WA Treasury's discussion paper on the issue. We also consider that the Commission should investigate obtaining independent advice on the accessibility of substitutable services rather than relying on State and Territory data. We consider this would give the assessment greater reliability and credibility, particularly for ED services.

Regarding the split of NAP and ED service expenditure, the ACT supports the Commission staff proposal to investigate methods of estimating annual NAP and ED service expenditure in order to calculate the split, though we consider that NWAU data should be reliable enough by the time of the implementation of the 2020 Review to be used for this purpose.

The ACT also supports the Commission staff proposal to consider assessing all hospital services in a single component. We consider that this proposal aligns with the intended direction of the NHCDC data collection as required by the IHPA and would simplify the Health assessment.

The ACT is supportive of the Commission staff proposals on cross-border use of Health services and note that our position on cross-border use of community health services is expanded upon further in the Cross-border section of the Other Disabilities chapter.

The ACT supports the proposal to investigate whether expenses for pharmaceuticals, medical aids and appliances and health administration should be included in the community health component or whether they relate mostly to delivery of hospital services.

Assessment Approach

Context

In the 2015 Review the Commission extended the direct assessment approach from admitted patient services to all health services. This replaced the so-called subtraction approach adopted in the 2010 Review. The basis of the subtraction approach was to assess the total of State/Territory and non-State/Territory (i.e. private and Commonwealth) expenditure on health services which could be provided by either sector and then subtract total actual non-State/Territory expenditure on these services to derive State and Territory expenditure needs. This approach was abandoned in the 2015 Review due mainly to the availability of improved usage and cost data for non-admitted services and a lack of reliable data for assessing total (State/Territory plus non-State/Territory) expenditure.

The direct approach assesses State and Territory expenditure only, with adjustments to reflect differences between the States and Territories in the availability of substitutable non-State/Territory services. Most States and Territories supported the move to this approach in the 2015 Review.

WA has proposed maintenance of a subtraction approach for non-admitted health services (including ED and community health services), focused on equalising outcomes rather than fiscal capacity and taking a very broad view of substitutable non-State/Territory services. Commission staff consider that equalisation of outcomes is beyond the scope of HFE and that the very broad view of substitutable services fails to take account of key factors such as income constraints on use of non-State/Territory services and access restrictions on State and Territory services.

Commission Staff Position

Staff propose to recommend that the Commission:

- Consider retaining the direct approach to assess all components of Health expenses in the 2020 Review rather than reverting to a subtraction approach because the direct approach utilises reliable data to directly assess State and Territory health spending and focuses on *What States Do* while appropriately recognising the influence of the non-State/Territory sector;
- Not scale the outcomes of the direct assessment method based on a very broad interpretation of what constitutes State/Territory-like services.

ACT Position

The ACT supports both of the Commission staff proposals.

The ACT considers that the direct approach is preferable to the subtraction approach because:

- The scope of the former is more appropriate, given that it applies an assessed distribution to State and Territory expenditure alone, rather than to the total of State/Territory and non-State/Territory expenditure; and
- The former makes better informed and more realistic assumptions about the actual substitutability of services.

A detailed exposition of our views on these issues is set out in the attached paper ([Attachment D](#)) on *Non-State Services in the Health Category – Paper by WA Treasury – ACT Comments* (March 2018).

Socio-demographic Composition

Context

The SDC assessments for NAP and community health currently use proxy indicators to assess spending for different population groups. Admitted patients data were used as a proxy for NAP expenses because of concerns about the reliability of the IHPA data provided through the NHDC.

At the time of the 2015 Review only limited national data were available for State and Territory provided community health services. Consequently, the SDC assessment for community health services was based on IHPA's data for ED triage categories four and five.

Commission Staff Position

Non-admitted Patient Services

Staff propose to recommend the Commission:

- Continue to use IHPA's NWAU data for the SDC assessments of admitted and ED services because the data provide a reliable basis for measuring the material factors which influence State and Territory spending on these services; and
- Use IHPA's NAP NWAU data for the SDC assessment of NAP expenses instead of admitted patient separations because the data should be sufficiently reliable by the 2020 Review and it will provide a better measure of the material factors which influence State and Territory spending on NAP services.

Community and Other Health Services

Staff propose to recommend the Commission:

- Investigate whether sufficiently comparable and reliable administrative data on community health services are available from States and Territories to build a national SDC profile for community health services; and
- In the absence of suitable data, staff will consider whether ED triage category four and five remain the best proxy for measuring the SDC disability for community health services.

ACT Position

The ACT supports both of the staff proposals.

We expect that the IHPA NWAU data will be sufficiently reliable by the time of the 2020-21 application year and will provide a better measure of the key drivers of State and Territory NAP expenditure than the current proxy measure.

The ACT is investigating whether we can supply activity data for community health services usage and cost, including socio-demographic factors, which could be included in development of a national usage profile for community health services.

However, the national data would need to be comprehensive and consistent across the States and Territories in its scope and cover a large proportion of the national population to be considered as a reliable basis for such a profile.

Remoteness and Service Delivery Scale

Context

The Commission relies on IHPA data to measure the influence of hospital and patient remoteness and hospital size on State and Territory costs. These factors are treated as loadings in the IHPA's determination of the NEP for activity-funded hospitals and the NEC for block-funded hospitals. Commission staff are concerned to ensure that the full costs of these factors are recognised in the assessment.

This includes examining the desirability of further refinements to the assessment to differentiate between remote and very remote areas and between under and over 85 year olds in the age group disaggregation.

Commission Staff Position

Staff propose to recommend the Commission:

- Note the changes to IHPA's adjustments for 2018-19 NWAU data, which will affect the assessment for the first time in the 2020 Review;
- Ensure all hospital remoteness and SDS costs for small rural block funded hospitals are recognised in the SDC assessments for hospital services (admitted patients, ED and NAP);
- Take steps to ensure that the proxy indicator used in the SDC assessment for community health adequately recognises remoteness and SDS costs;
- Re-test the materiality of splitting remote and very remote areas in the SDC assessments; and
- Re-test the materiality of splitting the older age group (75+ years) to have a 75-84 years age group and an 85+ age group.

ACT Position

The ACT supports the staff proposals, subject to our concerns about the validity and robustness of the SDS disability (see chapter on Geography Used by the Commission).

Substitutability

Context

Commission staff consider that identifying non-State/Territory services which affect what States and Territories spend requires evidence that State and Territory decisions about service provision are affected by the availability of non-State/Territory services. Other influences, such as eligibility for State and Territory services and income constraints on use of non-State/Territory services, must also be considered.

During the 2015 Review, consultants reviewed and advised on the levels of substitutability proposed by the Commission. Commission staff consider the choice of substitutability levels to be one of the main issues for this review. Staff also intend to investigate if the current indicators are the best available measure of the availability of substitutable services.

Commission Staff Position

Admitted Patient Services

Staff propose to recommend the Commission:

- Continue to recognise the influence of the non-State/Territory sector on admitted patient expenses using a direct assessment approach; and
- Confirm the level of substitutability and data used to calculate the non-State/Territory sector adjustment after staff analysis has been completed and the States and Territories have been consulted.

Emergency Department Services

Staff propose to recommend the Commission:

- Investigate if there are any new studies examining the relationship between GP and State and Territory provided ED services to support or otherwise indicate a different level of substitutability for ED services; and
- Investigate to what extent private ED services are substitutable with State and Territory ED services.

Non-admitted Patient Services

Staff propose to recommend the Commission:

- Confirm the current level of substitutability for NAP using the same approach used in the 2015 Review; and
- Investigate if service bundling or non-State/Territory allied health services have any implications for State and Territory provided NAP services.

Community Health Services

Staff propose to recommend the Commission:

- Re-estimate the substitutability level for community health using a bottom-up approach which examines each major service area on a case by case basis; and
- Investigate if bulk-billed GP benefits data, which is currently being used to estimate the availability of non-State/Territory community health services, is the best available indicator for this purpose.

ACT Position

The ACT generally agrees with the staff proposals in relation to substitutability. However, we have reservations about relying solely on information provided by the States and Territories to assess levels of substitutability, rather than on independent, clinically informed opinion. The Commission should consider seeking a review by consultants on this issue, as was carried out in the 2015 Review. Such a strategy would give greater credibility and reliability to the direct approach, particularly for the ED services estimate, where the Draft Assessment Paper signals an intention to identify new studies of the relationship between GP and ED services.

Cross-border Service Use

Context

The NHRA provides for the Commonwealth contribution to the States and Territories for public hospital services and is made to the State or Territory in which the service is provided (not to the State or Territory in which the patient is resident). It also includes bilateral agreements between States and Territories which require that each State and Territory is reimbursed by the State or Territory of residence for treatment of non-resident patients.

The Commission makes a cross-border adjustment to actual NHRA payments received so that the Commonwealth payments are counted against the capacity of the State or Territory of residence of patients. Similarly, State and Territory needs are assessed on the basis of the State or Territory of residence of patients, not on where the patient is treated.

Commission Staff Position

Staff propose to recommend the Commission:

- Note that the current arrangements ensure that the States and Territories are reimbursed for the cost of providing hospital services to residents of another State or Territory; and
- Review the approach to the cross-border assessment for community and other health services as outlined in the Draft Assessment Paper CGC 2018-01/25-S.

ACT Position

The ACT agrees that the current bilateral agreements between States under the NHRA provide for the *recurrent* costs of hospital services provided to residents of other States. However, they do not provide for the *capital* costs entailed in providing these services. Available statistics indicate that approximately 21% of ACT hospitalisations are NSW residents. Therefore the ACT contends that a cross-border allowance for this usage should be incorporated in the Physical Assets assessment.

The ACT supports the second proposal. Our position on the cross-border assessment for community health is set out in the chapter on Other Disabilities.

Non-hospital Patient Transport

Context

Commission staff intend to collect new data from the States and Territories on spending on aero-medical services and PATS. Staff want to ensure that there is no double counting of costs related to inter-hospital transfers, which are captured in IHPA's cost data.

Commission Staff Position

Staff propose to recommend the Commission retain the current method for assessing non-hospital patient transport expenses but collect new data to benchmark patient transport expenses and re-calculate the remote patient cost loading.

ACT Position

The ACT supports the staff proposal on the grounds of simplicity and transparency.

Other Expenses

Context

Commission staff intend to investigate whether expenses for pharmaceuticals, medical aids and appliances and health administration should be included in the community health component or whether they are related mostly to the delivery of hospital services. The preliminary staff view is that they should be included in the admitted patients component.

Commission Staff Position

Staff propose to recommend the Commission consider whether expenses for pharmaceuticals, medical aids and appliances and health administration not elsewhere classified should be included in the community and other health component or admitted patients component.

ACT Position

The ACT supports the proposal and will seek further information from our Health Directorate on the nature of these costs.

Component Expenses

Context

At the time of the 2015 Review, no data were available to reliably split ED and NAP services, so the Commission decided to split these expenses on a 50:50 basis. Commission staff have canvassed two alternatives for the 2020 Review:

- Use total NAP expenses from GFS and deduct ED expenses from the NHCDC or AIHW's Australian Health Expenditure publication to give a residual figure for NAP expenses.
- Use NWAU shares for ED and NAP to split the expenses.

Commission Staff Position

Staff propose to recommend the Commission consider options for deriving annual estimates of ED and NAP expenses.

ACT Position

The ACT supports the staff proposal, but considers that the NWAU data should be reliable enough by the time of the 2020 Review to be used to split the ED and NAP expenses.

User Charges

Context

In the Health assessment, all user charges are offset against expenses. 90 per cent of user charges relate to admitted patient services.

Revenue is classified as either fully compensable expenditure (e.g. sourced from the Department of Veterans' Affairs, Department of Defence, worker's compensation or motor vehicle third party claims) or partially compensable expenditure (e.g. sourced from health insurance funds and individuals).

Fully compensable expenses have no effect on States' and Territories' fiscal capacities, while partially compensable expenses have an effect, but less than that of services primarily funded by the States and Territories.

IHPA's admitted acute costing model recognises that private patients in public hospitals are less costly than public patients by including two adjustments: a private patient service adjustment and a private patient accommodation adjustment. This means that only the net cost to States and Territories of private patients is reflected in the NWAU data.

Some user charges also apply to community health services, but these cover only about 10 per cent of State and Territory costs. Exemptions and concessions apply to the most disadvantaged users of these services, so that the SDC profile of service users is likely to differ significantly from the profile of those paying user charges. However, staff consider that this difference is unlikely to have a material impact on the assessment.

Commission Staff Position

Staff propose to recommend the Commission continue to offset all user charges against expenses to maintain simplicity.

Commission staff contend that fully compensable patients have no effect on State and Territory fiscal capacities and it is appropriate to remove these expenses from the assessment. Only the residual cost of private patients in public hospitals affect State and Territory fiscal capacities and the NWAU data used in the SDC assessment recognises that private patients in public hospitals are less costly.

ACT Position

The ACT has set out a comprehensive position on user charges in the chapter on Other Revenue. We support the assessment and presentation of all user charges within the relevant expense assessments, rather than treating such charges under revenue. In general, we also support the netting off of user charges against expenses prior to differential assessment.

The ACT supports the staff proposal to offset all user charges against expenses.

Assessment Structure

Context

Use of NWAU data for all hospital services would enable the Commission to assess all hospital services in a single component, rather than in the separate components of admitted patients, NEP and ED. However, non-State/Territory sector adjustments would still need to be estimated separately for each of these components.

Commission Staff Position

Staff propose to recommend the Commission:

- Consider assessing all hospital services in a single component if IHPA's NWAU data for NAP services is considered sufficiently reliable by the time of the 2020 Review.

ACT Position

The ACT considers that this proposal aligns with the intended direction of the NHDC data collection as required by the IHPA and would offer substantial benefits in simplification. Subject to assurance about the likely quality of the NWAU data across all settings by 2020, we support the proposal.

Cultural and Linguistic Diversity

Context

IHPA recently completed a costing study to inform a policy decision for whether an adjustment is warranted to the NEP for CALD patients. It concluded that a CALD adjustment to the NEP model for sub-acute, ED or outpatient encounters could not be supported. It found that for acute admitted encounters, there was some evidence of CALD patients costing more than non-CALD patients; however the differences were small.

Among other findings, the study noted that there is no nationally consistent indicator for identifying CALD patients.

Commission Staff Position

Staff propose to recommend the Commission not include a cost adjustment for CALD patients, because any additional costs for CALD patients compared with non-CALD patients appear to be small.

ACT Position

The ACT supports the staff proposal, based on the findings of the IHPA costing study.

WELFARE

Summary

The Welfare assessment assesses States' and Territories' expenses on the provision of welfare services. The components of this assessment category are family and child services, aged care services, disability services, concessions and other general welfare.

- The ACT is supportive of all the Commission staff recommendations on the assessment of family and child services expenses, namely staying in contact with AIHW on the planned additions to the unit record database that the AIHW intends to introduce and the intention to use NSW data disaggregated by SES and region if it becomes available during the timeframe of the 2020 Review.
- The ACT requests Commission staff to conduct further analysis before concluding that a low SES measure can be used for assessment of any remaining State or Territory funding of aged care.
- The ACT agrees with the Commission staff recommendation to continue the dual assessment of disability services expenses, with one sub-component being for NDIS and the other for non-NDIS expenses.
 - The ACT agrees with the Commission staff proposal to assess NDIS expenses APC at full scheme implementation in the 2020 Review, subject to decisions taken on this issue in the 2019 Update.
 - The ACT requests Commission staff to conduct further analysis before concluding that a low SES measure can be used for assessment of State and Territory expenses on non-NDIS services. We contend that only if such analysis shows low SES to be a driver of use of non-NDIS services should the Commission staff proceed to merge the assessment of non-NDIS services with the other general welfare component, i.e. the conceptual case should be the guiding factor, not materiality considerations.
- The ACT agrees with the Commission staff proposal to retain the current assessment methodology for concessions.
- The ACT supports the Commission staff position on retaining homelessness related expenses within the other general welfare component of the Welfare assessment.
- The ACT supports the Commission staff proposal to measure low SES using ABS SEIFI data if it is available or by using the relative proportions of State and Territory populations in the bottom quintile of individual income as at the 2016 Census.
- The ACT agrees that user charges should be assessed EPC. However, the ACT considers that they should be presented in the Welfare assessment and not as Other Revenue, as it makes the assessment more transparent.

Context

The Welfare assessment comprises State and Territory expenses on the provision of the following Welfare services:

- Family and child services (dominated by child protection-related expenses);

- Aged care services;
- Services for people with a disability; and
- General welfare services (including concessions, assistance to the homeless, women's shelters and information, advice and referral services).

The assessment is performed in five separate components; the first three referred to above, concessions and other general welfare (a residual). States and Territories expended \$17.3 billion on welfare services in 2016-17, with family and child services and disability services together accounting for around 81 per cent of the expenses.

In the 2015 Review:

- Family and child services expenses, accounting for 33 per cent of all State and Territory expenditure on welfare services, were assessed based on AIHW child protection data. The disabilities used for the assessment reflected SDC influences namely, age, indigenous status, SES and remoteness. The PC's ROGS data was used to split expenses on this component between child protection and out of home care expenses, as indigenous use is materially different for the two types of child services. Other disabilities also included in assessing the family and child services expenses were regional costs, Wage Costs and SDS.
- Following changes from July 2011 (July 2015 for VIC) under the NHRA, WA was the only State or Territory with responsibility for basic community care and specialist disability services for older people (those aged over 65 or over 50 for indigenous). As a differential assessment was not material, aged care expenses were assessed EPC.
- Disability services, accounting for 48 per cent of all welfare expenses, were assessed by a dual service assessment model due to the transition to NDIS that was in progress – one for the NDIS and the other for State and Territory expenses associated with existing disability services. Since the change in federal financial relations due to NDIS was considered to be a major one, it was backcast.
 - State and Territory data were obtained annually on the projected share of disability expenses in the application year to split expenses between NDIS and existing disability services expenses. Commonwealth Department of Social Services data on the estimated number of 'younger people' (those aged under 65 or under 50 for indigenous) meeting the (full coverage) access requirements of the NDIS at full scheme were used as the driver of both NDIS expenses and existing disability services expenses. Cross-border, Wage Costs and regional costs influences were also taken into account in the existing disability services assessment.
 - When the NDIS becomes fully operational, State and Territory contributions will change from payments that take into account the number of people from each State and Territory in the scheme to EPC contributions based on State and Territory population shares at Census time. Since at that time State and Territory policies will have no impact on their NDIS expenses, the Commission proposed that State and Territory contributions would be assessed APC to take into account the annual change in population shares.

- The Commission also indicated that the dual assessment approach would be continued until the non-NDIS service provision assessment became non-material.
- Concessions were assessed using State and Territory shares of the number of pensioner concession card and health care card holders in each State and Territory, using Centrelink and Department of Veterans' Affairs data, as a proportion of State and Territory populations.
- Finally, the residual 'other general welfare' assessment, of which homelessness services accounted for the bulk of expenses, was assessed on the basis of the relative proportions of State and Territory populations considered to be of low SES. The latter was measured using the State and Territory populations in the bottom quintile of the ABS 2006 SEIFI, adjusted for changes in the relative proportions of State and Territory populations with concession cards between the 2006 and 2011 Censuses. Cross-border, Wage Costs and regional cost influences were also taken into account.
- Investment and depreciation expenses were taken into account in those respective assessments, with the assessment using the weighted service users of the Welfare assessment components.

The assessment of Welfare expenses redistributed \$61 million, or \$145 per capita in GST funding from the ACT in the 2018 Update.

Family and Child Services

Context

Commission staff consider that the current assessment approach for family and child services remains appropriate. They cite supporting facts in the paper to substantiate the choice of disabilities used in the assessment of this component.

Commission staff note that if data from NSW disaggregated by SES and region become available during the time-frame of the 2020 Review, they will integrate that into the assessment. The AIHW is also attempting to add CALD and disability dimensions to their unit record data. If such data become available in due course, Commission staff intend to explore the possible incorporation of extra disabilities. They suggest that a CALD measure could be the native language spoken at home or in parent country of birth, but they would also need a measure of CALD/non-CALD costs.

Commission Staff Position

Staff propose to recommend the Commission retain the current assessment methodology for family and child services but continue to monitor developments by the AIHW of their record database, including whether data might become available for NSW and to support a possible CALD and/or disability measure.

ACT Position

The ACT supports the Commission staff recommendation.

Aged Care

Context

Commission staff expect net expenses on aged care to be small by 2020-21, the application year of the 2020 Review, on the grounds that Home and Community Care and specialist disability services for older people have been taken up by the Commonwealth since July 2018. Staff propose to merge the expenses for aged care with expenses for other general welfare expenses and assess them using a low SES measure.

Commission Staff Position

Staff propose to recommend the Commission merge States' and Territories' residual aged care expenses with other general welfare expenses and assess them using a general low SES measure.

ACT Position

The Assessment Paper provides no evidence to support the case to merge residual aged care expenses with other general welfare expenses and assess them using a low SES measure.

The ACT's Community Services Directorate has advised that the ACT's policy for residual services in aged care does not involve means-testing. Consequently, people across all SES levels can be expected to use the services, unless the demand is such that waiting times are substantial. Hence, people from higher SES opt for services from private agencies.

The ACT requests Commission staff to conduct further analysis to substantiate the conceptual case for this proposal. If the Commission staff can share data on usage of the residual services which clearly shows people from low SES to be the predominant users of such services, the ACT would support this recommendation.

Disability Services – National Disability Insurance Scheme

Context

Commission staff note in the Draft Assessment Paper that WA's expenses needed to be made consistent with those of the other States and Territories. However, WA has now also signed the same agreement on NDIS that other States and Territories have, suggesting that the changes were no longer required.

In view of the PC's October 2017 review of NDIS costs, Commission staff contend that the implementation of the full scheme could be delayed beyond the dates anticipated in the Heads of Agreement. Hence, staff intend to raise the assessment of NDIS expenses as a part of the 2019 Update new issues process.

Commission Staff Position

Staff propose to recommend the Commission assess NDIS expenses APC at full scheme implementation in the 2020 Review, subject to decisions on this issue to be taken in the 2019 Update.

ACT Position

The ACT supports the Commission staff recommendation.

Disability Services – Non-National Disability Insurance Scheme

Context

The Commission stated in its 2015 Review report that, upon full implementation of the NDIS, it would continue assessing non-NDIS disability services separately until the expenditure ceased to be material. Commission staff have tested the materiality of the current non-NDIS disability expenses assessment with its most likely alternative assessment in the other general welfare component, using low SES as the disability. In either approach, it does not result in a material assessment, using the \$35 per capita materiality threshold.

Commission staff consider that after the NDIS is fully implemented, any non-NDIS State and Territory expenses would target the gap between NDIS and mainstream services and support people who cannot access NDIS services and are also not able to afford relatively costly private care, i.e. proportion of people in the low SES groups could be used as a disability.

Similar to the NDIS expenses, Commission staff intend to raise the issue of non-NDIS expenses as a part of the 2019 Update new issues process.

Commission Staff Position

Staff propose to recommend the Commission re-allocate non-NDIS expenses to the other general welfare component and assess them using the same measure of low SES as that used for other general welfare expenses after the full implementation of NDIS, subject to decisions on this issue taken in the 2019 Update.

ACT Position

The ACT contends that as far as combining any component of an assessment with another is concerned, the underlying conceptual case has to be similar for both. Whether the result is material or not is completely incidental and cannot be considered to be a reason for combining components of assessments.

That said, the ACT requests Commission staff to conduct further analysis on this topic before concluding that a low SES measure can be used for assessment.

The ACT's Community Services Directorate have advised that the ACT's policy for non-NDIS services does not involve means-testing. Since there is no means-testing, people across all SES levels can be expected to use the services, unless the demand is such that waiting times are substantial and hence, people from higher SES opt for services from private agencies. If the Commission staff can share data on usage of the non-NDIS services which clearly shows people from low SES to be the predominant users of such services, the ACT would support this recommendation.

Concessions

Context

Commission staff consider that an assessment based on the number of pensioner concession cards and health care card holders in each State and Territory as a proportion of State and Territory population continues to hold merit as those numbers are relevant and policy neutral indicators.

Commission Staff Position

Staff propose to recommend the Commission retain the current assessment methodology for concessions.

ACT Position

The ACT supports the Commission staff recommendation.

Other General Welfare

Context

Homelessness related expenses were the biggest sub-component of expenses in the other general welfare component in the 2015 Review. However, as services to the homeless can be considered to be another facet of services for social housing, Commission staff considered the option of re-allocating homelessness expenses to the Housing assessment. Their investigation has led them to conclude that homelessness needs differ from the needs in social housing, a perspective that TAS also shared in their response to the Commission Staff Research Paper *What States Do - Housing Services*.

As an example, services provided to the homeless can include counselling and other services related to drug and alcohol abuse, gambling addiction, family and relationship breakdown, domestic violence and physical and sexual abuse, indicating that such causes could be possible drivers for homelessness. Hence, staff consider that it would not be accurate to apply the disabilities for social housing services to homelessness expenses and propose to retain homelessness expenses in the Welfare assessment.

Needs in this component are assessed using a low SES measure.

In the 2015 Review, ABS SEIFI developed using 2006 Census data was used to measure low SES. If ABS SEIFI data is updated for the 2016 Census, staff propose to use that data in assessing expenses in the other general welfare component. If updated SEIFI data is not available, staff propose to use the relative proportion of State and Territory populations in the bottom quintile of individual income as measured at the 2016 Census, consistent with the SEIFI measure.

Commission Staff Position

Staff propose to recommend the Commission:

- Retain homelessness related expenses within the other general welfare component of the Welfare assessment; and
- If the ABS updates SEIFI, use it to measure needs for other general welfare expenses. If an updated SEIFI is not available for the 2020 Review, use the relative proportions of State and Territory populations in the bottom quintile of the 2016 Census individual income.

ACT Position

The ACT supports the Commission staff position on retaining homelessness related expenses within the other general welfare component of the Welfare assessment. We concur that homeless needs differ from the needs in social housing, based on the causes cited above and on input received from our Community Services Directorate.

The ACT agrees with the Commission staff recommendation on the use of ABS SEIFI data or the alternate option suggested.

User Charges

Context

Commission staff contend that user charges are not impacted by the same disabilities used to assess the various components of welfare expenses. The amounts are small and a significant proportion of them relate to aged care services which have no impact on GST shares.

Commission Staff Position

Staff propose to recommend the Commission assess revenues from user charges on an EPC basis in the Other Revenue assessment.

ACT Position

The ACT agrees that user charges for different components of welfare expenses should be assessed on an EPC basis. However, we consider that user charges should be retained in the Welfare assessment instead of being moved to Other Revenue as that makes the assessment more transparent.

HOUSING

Summary

The Housing assessment captures the cost to States of providing housing services. Under the 2015 Review methodology, housing expenditure is assessed on service expenses, revenue and first home owner expenses. Data on first home owner expenses are obtained through data requests to the States.

The ACT is generally supportive of the Commission staff proposals.

Regarding the Commission staff proposal to scale Census data to match AIHW estimates of the total number of social and community residences, the ACT considers that there is sound evidence of underreporting of community housing residences in the 2016 Census and supports the Commission staff proposal to scale 2016 Census data to match AIHW estimates of the total number of social and community housing residences.

The ACT also supports the Commission staff position not to adjust the Housing assessment for the cost of land, as an adjustment in the Housing assessment for the cost of land acquisition would likely be too small to have a material impact on the GST distribution.

The ACT considers that Commission staff should review the availability of data sources for State and Territory expenses on affordable housing and will provide a final response in a supplementary submission. The ACT also considers that Commission staff should review the availability of data on first home buyers in general (i.e. not limited to those eligible for State and Territory grants or concessions) to establish whether a suitable measure for an assessment of FHOGs can be identified. We will provide a final response in a supplementary submission.

The ACT also supports the Commission proposal to retain the indigenous and location cost weights and to update them with more recent data.

Context

The Housing assessment captures the cost to States and Territories of providing housing services. These services include the provision of public housing and subsidies to community housing providers and private rental assistance. Further, the Housing assessment also captures FHOGs, concessions for first home owners and other home purchase assistance. The Housing assessment does not include accommodation of State and Territory government employees, the provision of residences for special needs persons, including youth and disabled housing, or homelessness services.

Under the 2015 Review methodology, housing expenditure is assessed on gross operating expenses net of depreciation (service expenses), revenue and first home owner expenses. Service expenses are assessed on the basis of ABS Census data on the number of households nationally in social housing by income, indigenous status and remoteness. The distribution between States and Territories is assessed on the basis of the proportion of their populations which are in sociodemographic groups which make greater use of social housing.

Maintenance costs are assumed to be 25 per cent of service expenses and are assessed on the basis of housing location and construction costs. Revenue is also assessed on the basis of ABS data on household income, indigenous status and location.

First home owner expenses are assessed on an EPC basis due to the Commission being unable to identify a policy neutral cost driver. Data on first home owner expenses are obtained through data requests to the States and Territories.

The Housing assessment redistributed \$18 million, or \$42 per capita of GST funding from the ACT in the 2018 Update.

Commission Staff Position

Commission staff, in Draft Assessment Paper 2018-01/14-S, have identified several issues with the 2015 Review methodology and have proposed approaches for addressing these issues.

Commission staff have identified ABS 2016 Census data and data from the AIHW's *Housing Assistance in Australia Reports* as possible sources for the Housing assessment. However, the Commission notes significant discrepancies between the datasets. Commission staff have concluded that AIHW data is more accurate at the macro level, providing more complete information on the total number of social housing dwellings, particularly for indigenous community housing, while the 2016 Census data is more reliable in identifying the demographic characteristics of households in social housing.

Commission staff propose to alter the 2015 Review methodology of only using Census data, by combining Census and AIHW data to capture the strengths of both datasets. The proposal is to scale the 2016 Census data to match the total number of social housing dwellings identified in the AIHW data and use the 2016 Census data to assess State and Territory SDC and therefore State and Territory needs. Likewise, Commission staff also propose to extend this scaling exercise to the revenue component of the Housing assessment by scaling 2016 Census household data to AIHW household numbers.

Commission staff have also responded to a proposal by NSW for the Housing assessment to incorporate the cost of land, on the basis that land acquisition is the most significant expense in the provision of social housing in urban areas. Commission staff responded that land costs would not impact recurrent expenditure on housing services and that, as per ABS GFS data, the cost of land acquisition, particularly when netted against revenue from land sales, would be too small for a land cost assessment to be material. Consequently, Commission staff propose not to differentially assess housing related land costs, though States and Territories have been invited to further develop a case for such a disability.

An increased focus by the States and Territories and the Commonwealth Government on affordable housing measures has also been noted by Commission staff. Commission staff have indicated however that they have no information on State and Territory spending on affordable housing, stating that they assume the expense would be small compared to social housing expenses. Commission staff have also noted that most affordable housing is supported by the Commonwealth Government through NRAS rather than by States and Territories and that there are significant inconsistencies in reporting on NRAS dwellings between States and Territories. On this basis, Commission staff propose not to pursue a separate assessment of affordable housing expenses.

Commission staff have also proposed to retain the EPC assessment of FHOs and stamp duty concessions on policy neutrality grounds and to update the indigenous cost weight and location factor using up to date State and Territory data.

ACT Position

The ACT is generally supportive of the Commission staff proposals.

Regarding the Commission staff proposal to scale Census data to match AIHW estimates of the total number of social and community residences, the ACT agrees with the Commission staff assessment of the 2016 Census data. As alluded to by Commission staff, the ACT notes that the number of people reported to live in housing cooperatives or residences provided by community or church groups fell from 52,401 nationally in the 2011 Census to 52,020 in the 2016 Census.

This contrasts with observed general growth in the community housing sector, indicated by the Sector Capacity Prospectus 2017-18, prepared by PowerHousing Australia, a network of 30 community housing providers. The Sector Capacity Prospectus 2017-18 shows an increase of 45 per cent in the number of units of accommodation being managed by PowerHousing members in the four years to June 2017. Intuitively, growth in the community housing sector would be reflected in an increase in the number of households that reside in community housing, however the 2016 Census data does not corroborate this.

Moreover, the ACT notes the discrepancy identified by Commission staff between the 2016 Census data and AIHW data. The ACT notes that 57,901 households resided in community housing according to the AIHW Housing Assistance in Australia 2012 Report. This compares to 80,225 in the AIHW Housing Assistance in Australia 2017 Report; representing a 38.6 per cent increase in the number of households reported by the AIHW to reside in community housing over this timeframe. This compares to a 0.7 per cent decrease in those reported in the 2016 Census relative to the 2011 Census.

Moreover, the discrepancy between the AIHW data increased between the 2011 Census and 2016 Census, with the 2011 Census having 90.5 per cent of the reported households residing in community housing in the Housing Assistance in Australia 2012 Report, compared with 64.8 per cent of those reported in the Housing Assistance in Australia 2017 Report for the 2016 Census. The ACT considers that these growing discrepancies are sound evidence of underreporting in the 2016 Census.

The ACT notes however that the AIHW data has its own issues. As noted in the AIHW data quality statements, data for individual States and Territories for community housing, private rent assistance, public rental housing and State/Territory owned and managed indigenous housing may not be comparable between jurisdictions or across reporting periods. This is due principally to the variability in the scope of State and Territory government programs reported in the data collection. The ACT considers however, given AIHW data would only be used to determine the total number of households in public or community housing, that this should have a limited impact on the assessment.

All considered, the ACT regards the Commission staff proposal to scale 2016 Census data to match AIHW estimates of the total number of social and community residences to be sound and we are supportive of the proposal as a means to mitigate the apparent discrepancy between the 2016 Census data and other data sources.

The ACT also supports the Commission staff position on the NSW proposal to adjust the Housing assessment for the cost of land.

As stated by Commission staff, the cost of land acquisition does not place further ongoing expenses on States and Territories for the provision of housing services, with the possible exception of the cost of servicing additional financial liabilities due to greater borrowing needs. However, the ACT notes that the cost of borrowing is already captured in the physical and financial assets assessment. Moreover, as identified by the Commission, the quantum of land acquisition expenses that are directly related to housing are not likely to be significant enough to warrant a differential assessment.

The ACT thus considers that incorporating an adjustment in the Housing assessment for the cost of land acquisition would not cause a material impact on the GST distribution. On this basis, the ACT supports the Commission staff position not to differentially assess housing related land acquisition costs.

The ACT considers that Commission staff should review the availability of data sources for State and Territory expenses on affordable housing which the Commission could use for assessment purposes. We reserve our position on this issue and will include a final response in a supplementary submission to be provided to the Commission. The ACT also considers that Commission staff should review the availability of data on first home buyers in general (i.e. not limited to those eligible for State and Territory grants or concessions) to establish whether a suitable measure for an assessment of FHOGs can be identified. We reserve our position on this issue and will include a final response in a supplementary submission to be provided to the Commission.

The ACT also supports the Commission proposal to retain the indigenous and location cost weights and to update them with more recent data. The ACT recognises that remoteness and indigeneity place further cost pressures on the provision of State and Territory government services, including housing. The ACT considers that these costs should be acknowledged in the equalisation process and supports the use of the most up to date data available to ensure that the Housing assessment is as contemporaneous and accurate as possible.

SERVICES TO COMMUNITIES

Summary

The Services to Communities assessment captures the cost to States of the provision of a variety of community services relating to administration, development, essential services and environmental protection. The assessment is separated into three components:

- Utilities Subsidies;
- Community Development and Amenities; and
- Protection of the Environment.

Under the Utilities Subsidies component, the ACT supports the Commission staff proposal to disaggregate the electricity subsidies and water subsidies sub-components into individual assessments. We also support the proposed Commission staff examination of adjustments to the electricity subsidy sub-component for fuel type, noting that there is a significant degree of State and Territory policy choice in the generation mix of both regulated and unregulated electricity networks.

The ACT does not oppose the Commission staff proposal to only assess subsidies for communities of a given remoteness and size, but considers that the proposed method has a risk of being arbitrary and may not capture other factors which influence the feasibility of cost recovery. The ACT considers that the Commission's proposal requires more information in order to be properly analysed. The ACT also considers there is no conceptual basis for an indigeneity adjustment for utilities subsidies.

Under the Community Development and Amenities component, the ACT is supportive of the Commission staff proposal to verify the quality of GFS data for estimating annual expenses and further supports the Commission staff proposal to disaggregate indigenous and non-indigenous community development expenses. The ACT is also supportive of non-indigenous community development expenses being assessed on an EPC basis.

Likewise, the ACT supports the ongoing assessment of community amenities expenses on an EPC basis. However, the ACT does not support removing non-indigenous community development and community amenities expenses from the Services to Communities assessment and transferring them to the Other Expenses assessment on transparency and consistency grounds.

The ACT supports the proposal to continue to assess Protection of the Environment expenses on an EPC basis. The ACT is also open to the proposal to apply a regional cost loading to Protection of the Environment expenses. The ACT also supports continuing to apply a Wage Costs assessment to Protection of the Environment expenses and to not assess the impact of private environmental protection services on State and Territory expenses. The ACT does not however support the Commission staff proposal to assess Protection of the Environment expenses under the Other Expenses assessment due to transparency concerns. Likewise, the ACT does not support the Commission proposal to assess Protection of the Environment user charges under the Other Revenue assessment on transparency grounds.

Context

The Services to Communities assessment captures the cost to States and Territories of the provision of a variety of community services relating to administration, development, essential services and environmental protection. The assessment is separated into three components:

- Utilities Subsidies;
- Community Development and Amenities; and
- Protection of the Environment.

The Services to Communities assessment redistributed \$24 million, or \$58 per capita in GST revenue from the ACT in the 2018 Update.

Utilities Subsidies

Context

The Utilities Subsidies component of the Services to Communities assessment captures the expenses incurred by States and Territories in supporting electricity, water and sewerage service providers to reduce the cost of these services to consumers. Such subsidies are divided by the Commission into two sub-components:

- Common subsidies, which are subsidies that lower the service cost below the cost of delivery, principally in metropolitan areas; and
- Differential subsidies, which are additional subsidies that lower the service cost in areas outside metropolitan areas. In practice, differential subsidies appear in the form of uniform tariffs.

The Utilities Subsidies category does not capture the cost to States and Territories of providing concessions on utilities to certain demographic groups or organisations, such as pensioners or religious buildings. These expenses are addressed in the Welfare assessment. Further, the Utilities Subsidies category does not assess utilities regulation costs, which are captured in the Services to Industry assessment.

Under the 2015 Review methodology, total utilities subsidy costs are allocated between common and differential subsidies on a 50/50 split. A 50/50 split is used based on data from the States and Territories indicating that 40 per cent of utility subsidy expenses were for remote communities with populations less than 1,000 (i.e. 40 per cent of utility subsidy expenses were on differential subsidies for communities with populations less than 1,000). The Commission increased the split from a notional 40/60 to 50/50 in order to capture remote communities with populations above 1,000.

Common subsidies are assessed on an EPC basis, while differential subsidies are differentially assessed on the basis of the number of residents per State and Territory in remote or very remote areas in communities with populations between 50 and 1,000 people. Regional and SDS cost gradients, both discounted by 25 per cent, are also applied.

The Utilities Subsidies component of the Services to Communities assessment redistributed \$17 million, or \$41 per capita in GST from the ACT in the 2018 Update.

Commission Staff Position

In Draft Assessment Paper 2018-01/15-S, the Commission proposes to separate water and electricity subsidies into individual assessments. This contrasts with the 2015 Review approach of a joint assessment of electricity and water subsidies and is proposed on the basis that national average subsidies for water and electricity services are likely to differ significantly. The water subsidies sub-component would also be inclusive of sewerage subsidies.

Commission staff also propose to change the manner in which assessable costs are determined, proposing to determine a point, on the basis of community size and remoteness, at which full cost recovery for water and electricity services is not feasible and only differentially assessing subsidies for communities which fit the Commission's community size and remoteness criteria; what Commission staff are calling "unavoidably high costs". Any additional subsidy provided by States and Territories would be deemed a policy choice and not be differentially assessed.

Further, this would also involve a discontinuation of the regional cost weight and SDS factor for utilities subsidies, as the new assessment format would already capture these disabilities. Commission staff note that the proposed new assessment format has been designed on the basis of electricity subsidy data, but it is intended that a similar format will apply to water subsidies as well.

Commission staff have noted that their analysis of State and Territory electricity subsidy data is incomplete and expect their work to be completed by the end of June 2018. Commission staff also indicate their intention to analyse and possibly propose further changes to the electricity subsidy sub-component to adjust the assessment for indigenous status and generator fuel type, though Commission staff consider these issues to be of lesser importance to the assessment. Commission staff further note that they have not yet begun to analyse State and Territory water subsidy data and expect to do so during the second half of 2018.

Commission staff have also considered the impact of non-State/Territory providers of electricity, water and sewerage services on State and Territory utilities subsidies costs. Commission staff concluded that it would be difficult to quantify the effect of non-State/Territory spending on State and Territory subsidies and thus propose not to assess the effect of the non-State/Territory sector on utilities subsidies.

ACT Position

The ACT supports the Commission staff proposal to disaggregate the electricity subsidies and water subsidies sub-components into individual assessments. The ACT agrees with the Commission staff argument that electricity and water subsidies do not necessarily have the same average policies or cost drivers. The ACT notes that this is reinforced by the significant differences in regulation and market structure between electricity services and water services, with significant elements of the national electricity market being owned privately while water services are generally provided by State and Territory owned enterprises or local councils. The ACT also considers the Commission proposal to jointly assess sewerage services and water services under the same sub-category to be reasonable, as most water service providers also provide sewerage services.

The ACT considers that the Commission staff proposal would improve the accuracy of the assessment and improve the assessment's conformity to the principle of *What States Do*.

The ACT does not oppose proposed Commission staff efforts to examine adjustments to the electricity subsidy sub-component for fuel type. However, the ACT notes that there is a significant degree of State and Territory policy choice in the generation mix of both regulated and unregulated electricity networks. Evidence of this includes the NT's ongoing Solar Energy Transformation Program, which is resulting in a widespread replacement of diesel generators in remote NT communities with fuel-less solar photovoltaic cells. The ACT considers that due care must be taken by the Commission in determining a policy neutral cost driver for generation fuel costs as part of its analysis.

The ACT also does not oppose the Commission staff proposal to only assess utility subsidies for unavoidably high costs. However, we have some concerns that the combination of community size and remoteness decided upon by the Commission to be the point beyond which cost recovery is not feasible has a risk of being arbitrary and may not capture other factors which influence the feasibility of cost recovery, including the socioeconomic status of communities, the value of assets or future investment requirements.

The ACT considers that the Commission's proposal requires more information on the process that would be used to determine the point at which cost recovery is unfeasible in order to be properly analysed. The ACT does acknowledge that the proposed new assessment format would capture the impact of remoteness and community size on costs if implemented and in principle would support the removal of the regional cost weight and SDS factor if the Commission staff proposal were adopted.

Noting that Commission staff have stated that their analysis of State and Territory subsidy data is incomplete, the ACT considers that a supplementary paper on this proposal is needed with further proposed methodological details when Commission staff have completed their analysis.

Further, the ACT does not see a conceptual basis for an indigeneity adjustment in the Utilities Subsidies component of the Services to Communities assessment. The ACT acknowledges that indigenous communities generally have higher utilities services costs than non-indigenous communities, given that they are concentrated in regional and remote areas. Thus, indigenous communities do require a higher level of subsidy. However, the ACT notes that these additional costs are already captured in the regional cost and SDS disabilities.

The ACT considers that an additional disability for indigeneity would only be conceptually coherent if there were evidence that indigenous communities place more demand on electricity, water and sewerage networks than non-indigenous communities of comparable remoteness and size. This would necessitate a higher standard of infrastructure in indigenous communities relative to non-indigenous communities in order to ensure supply stability and thus would increase the cost of service provision. The ACT considers that there is no evidence that this is the case.

Noting the Commission's difficulty in quantifying the impact of non-State/Territory provision of utilities services on State and Territory subsidies, the ACT also supports the Commission staff proposal to not assess the effect of the non-State/Territory sector on utilities subsidies.

Community Development and Amenities

Context

The Community Development and Amenities component of the Services to Communities assessment captures the cost to States and Territories of community development, including land use planning and administration, zoning law administration, building standard administration and public facilities planning. The component also captures the cost to States and Territories of the design, installation, operation and maintenance of public amenities such as street lights, public toilets and cemeteries. Community development and community amenities are each treated as sub-components.

The community development sub-component is separated into two further sub-components: indigenous community development and non-indigenous community development. This recognises that States and Territories spend more per capita on community development in indigenous communities, providing additional administrative and governance support to indigenous communities, as well as the greater needs of indigenous communities due to their remoteness, low populations and low income levels.

Under the 2015 Review methodology, indigenous community development expenses are assessed on the basis of State and Territory shares of the national number of indigenous people living in discrete indigenous communities. Commission staff define discrete indigenous communities as ABS SA1s with populations that are more than 50 per cent indigenous. Non-indigenous community development expenses are assessed on the basis of the remaining population, though in practice this amounts to an EPC assessment.

Community amenities costs are assessed on an EPC basis, as the Commission considers this to be the most appropriate way of allocating expenses.

The Community Development and Amenities Component of the Services to Communities assessment redistributed \$8 million, or \$19 per capita in GST funding from the ACT in the 2018 Update.

Commission Staff Position

Commission staff, in Draft Assessment Paper 2018-01/15-S, have identified indigenous community expenses to be the primary point of contention in the Community Development and Amenities category; particularly in regards to the identification of relevant expenses for the assessment.

Commission staff propose to collect data on indigenous community development expenses from the States and Territories in order to evaluate the quality of GFS data and determine the best approach for estimating annual expenses.

Commission staff also propose to expand the scope of the indigenous community expenses sub-category to include general revenue grants made by States and Territories to local councils with predominantly indigenous populations, arguing that these expenses are primarily driven by the needs of indigenous communities. Commission staff also propose to continue to use the indigenous population living in discrete indigenous communities, adjusted for Wage Costs and regional costs, as the basis for assessing indigenous community development expenditure needs and to continue to define discrete indigenous communities as SA1s with populations that are more than 50 per cent indigenous.

At a presentational level, Commission staff further propose to disaggregate indigenous community development expenses from non-indigenous community development expenses; continuing to assess indigenous community development expenses under the Services to Communities assessment, but as a discrete category.

Conversely, Commission staff propose to simplify the assessment of non-indigenous community development expenses by assessing them on an EPC basis. Commission staff further propose to remove the non-indigenous community development sub-category from the Services to Communities assessment and instead assess these expenses under the Other Expenses assessment. This proposal is on the basis that most other expenses that are assessed on an EPC basis are also included in the Other Expenses assessment.

Similarly, Commission staff propose to continue to assess community amenities expenses on an EPC basis and to move the sub-category from the Services to Communities assessment to the Other Expenses assessment. Commission staff also propose to continue to apply wage cost and regional cost disabilities to all sub-components of community development and amenities expenses.

ACT Position

The ACT supports the Commission staff proposal to verify the quality of GFS data for estimating annual expenses. The ACT considers that such a process would strengthen the accuracy, transparency and validity of the assessment, irrespective of whether GFS data is confirmed as the best available data source or if an alternative is proposed. The ACT does consider however that GFS data is generally sound and suitable for the Commission's needs.

The ACT further supports the Commission staff proposal to disaggregate indigenous and non-indigenous community development expenses. While this would only be a presentational issue and have no effect on the GST distribution, the ACT considers that separating the two elements of the community development sub-category would improve the transparency of the assessment, as there are different assessment methodologies for the two elements both in the 2015 Review methodology and the proposed 2020 Review methodology.

Noting that assessed expenses for non-indigenous community development generally follow an EPC distribution despite its current differential assessment, the ACT is supportive of these expenses being assessed on an EPC basis. Likewise, the ACT supports the ongoing assessment of community amenities expenses on an EPC basis. However, the ACT does not support removing non-indigenous community development and community amenities expenses from the Services to Communities assessment and transferring them to the Other Expenses assessment. As previously noted, the ACT considers that this would reduce the transparency of the assessment and GST distribution. The ACT considers that expenses presented under the Other Expenses assessment should be minimised.

Protection of the Environment

Context

The Protection of the Environment component of the Services to Communities assessment captures the cost to States and Territories of the monitoring, management and protection of the natural environment and the administration of related standards and regulations. These services include monitoring and regulation of air and water quality, pollution and erosion control, flood mitigation, waste disposal, environmental research, industrial chemical management and biodiversity conservation.

Environmental expenses related to major infrastructure projects are not assessed under this component, but are captured in the Services to Industry assessment instead.

Under the 2015 Review methodology, Protection of the Environment expenses are calculated as a residual of Services to Communities after Utilities Subsidies and Community Development and Amenities are calculated. Protection of the Environment expenses are assessed on an EPC basis, due to difficulty in identifying cost drivers. A wage cost disability is also applied to Protection of the Environment expenses, but a regional cost disability is not, as the location of service provision is not always clearly identifiable.

The Protection of the Environment component of the Services to Communities assessment redistributed \$1 million, or \$2 per capita in GST funding to the ACT in the 2018 Update.

Commission Staff Position

Commission staff, in Draft Assessment Paper 2018-01/15-S, do not propose major changes to the methodology used to assess Protection of the Environment expenses. Commission staff propose to continue to assess the expenses on an EPC basis, noting that while new GFS classifications make it possible to identify four broad categories of environmental protection services, the range of specific activities in these categories varies significantly.

Commission staff argue that this makes identifying cost drivers for each of the four GFS categories impractical and that even if it were, the expenses in the Protection of the Environment category are so small that a disaggregated assessment would likely be immaterial for each sub-category.

Commission staff further propose to continue to apply a wage cost disability to Protection of the Environment expenses, though they also note that some environmental protection services, such as national parks and wildlife services, can be determined to be provided primarily in regional areas. Consequently, Commission staff are also considering whether to apply a regional cost disability to some or all Protection of the Environment expenses.

From a presentation viewpoint, Commission staff also propose to remove Protection of the Environment expenses from the Services to Communities assessment and assess them under the Other Expenses assessment instead. Commission staff make this proposal on the basis that most expenses that are assessed on an EPC basis are also assessed under the Other Expenses assessment.

Commission staff also considered a possible assessment of the impact of private environmental protection services on State and Territory needs. Commission staff argued that there is not a clear differential level of private environmental protection services across States and Territories and that creating an assessment would be impractical. On this basis, Commission staff propose not to assess the impact of private environmental protection service providers on the Protection of the Environment costs to States and Territories.

ACT Position

The ACT is generally supportive of the Commission staff proposals on Protection of the Environment expenses.

The ACT, noting the lack of identifiable cost drivers as expressed by Commission staff, supports the proposal to continue to assess Protection of the Environment expenses on an EPC basis.

The ACT further notes that the expenses for protection of the environment appear to be small, amounting to \$2.2 billion, or \$94 per capita nationally in 2013-14 as per the 2015 Review. Therefore, a differential assessment of these expenses would likely have a minimal impact on the GST distribution.

Noting the development of new GFS classifications for environmental protection services, the ACT would also welcome the use of the new classifications to determine total expenditure on environmental protection. The ACT considers the 2015 Review approach of calculating Protection of the Environment expenses as a residual of Services to Communities expenses after Utilities Subsidies are calculated to be unsatisfactory and that the new GFS classifications should make it possible to use actual State and Territory expenditure data for the assessment.

The ACT is also open to the proposal to apply a regional cost loading to protection of the environment expenses. The ACT acknowledges that certain environmental services are more prevalent in remote or regional areas, such as forest management, while other services are more prevalent in inner or outer metropolitan areas, such as noise pollution monitoring. The ACT considers that there is a conceptual basis for applying a regional cost loading to protection of the environment expenses, but notes that identifying the quantum of expenses in each regional classification could be difficult. As with the Commission staff proposal to assess Protection of the Environment expenses on an EPC basis, GFS classifications may not provide sufficient information to allow the identification of the exact services that were provided by each State and Territory and how much of that expenditure occurred in different regional areas.

The ACT does not support the Commission staff proposal to assess Protection of the Environment expenses under the Other Expenses assessment. Consistent with our position on similar proposals in other assessments, the ACT considers that assessing expenditure under Other Expenses reduces the transparency of the assessment. The ACT considers that presentation of expenses under the Other Expenses assessment should be minimised.

While the ACT did suggest that the Commission investigate the possibility of assessing the impact of private environmental protection services on State and Territory needs, given the difficulties in developing such an assessment identified by the Commission, the ACT is supportive of the Commission proposal not to assess the impact of private services. The ACT is also supportive of continuing to apply a Wage Costs assessment to Protection of the Environment expenses.

User Charges

Context

User charges assessed under the Services to Communities assessment are regulatory charges related to Community Development and Protection of the Environment.

Under the 2015 Review methodology, services which generate user charges are assessed on an EPC basis, with user charges for Protection of the Environment netted against expenses, while user charges for Community Development and Amenities are not.

Commission Staff Position

In order to simplify the assessment, Commission staff, in Draft Assessment Paper 2018-01/15-S, propose to remove all user charges under the 2015 Review methodology from the Services to Communities assessment and assess them under the Other Revenue assessment instead. These user charges would continue to be assessed on an EPC basis. This is a presentational issue and would have no impact on the GST distribution.

ACT Position

While the ACT supports the Commission staff efforts to simplify assessments when practical, the ACT does not support the Commission staff proposal to assess Services to Communities user charges under the Other Revenue assessment. The ACT considers that this would reduce the transparency of the Services to Communities assessment and that the revenues assessed in the Other Revenue assessment should be minimised. The ACT supports the continuation of the 2015 Review treatment of user charges for Services to Communities.

JUSTICE

Summary

The Justice assessment encompasses State and Territory expenditure on police, civil and criminal courts, other legal services and corrective services. However, it does not include expenses related to fire-protection and State and Territory emergency services.

There are three components of assessment in the Justice assessment – police, courts and prisons.

- The ACT supports the Commission staff position of developing a new approach to determine the assessed expenses for policing.
- We request Commission staff to further investigate the relative proportions of criminal court and civil court expenses since the data that have been used to determine the ratio seem to have some anomalies. At the same time, we support the Commission staff recommendations on assessing criminal legal matters using use rates based on State and Territory data and not applying any cost-weights to population groups.
- The ACT broadly supports the Commission staff recommendation to continue with the method followed in the 2015 Review for the assessment of corrective services expenditure.
 - However, the ACT contends that use of SES data for courts as a proxy of SES data for prisoners is not completely accurate. Hence, the ACT considers that the assessment for expenses on prisons should be discounted by 25 per cent.
- The ACT's views on the Commission staff recommendation to assess user charges EPC in the Other Revenue assessment are:
 - We understand that drivers of user charges are different from those for use of Justice services and are also quite varied in nature. Hence, the ACT supports an EPC assessment of user charges.
 - However, we contend that the user charges assessment should be presented in the Justice assessment since it improves transparency of the assessment.
- We support all the remaining Commission staff recommendations on applying the Wage Costs disability in the Justice assessment, retaining the 2015 Review method for regional costs and SDS and assessing the influence of the use of AFP services by the ACT on our police expenses.

Context

The Justice assessment encompasses State and Territory expenditure on police, civil and criminal courts, other legal services and corrective services. However, it does not include expenses related to fire-protection and State and Territory emergency services (expenses of \$3.8 billion in 2016-17), which are assessed in the Other Expenses assessment. User charges for justice services are assessed EPC in the Other Revenue assessment.

States and Territories expended \$19.3 billion in 2016-17 on the provision of Justice services.

Police services accounted for about 53 per cent of that (\$10.3 billion) with the rest almost equally split between courts and prisons (\$4.4 billion (23 per cent) and \$4.5 billion (24 per cent)).

There are three components in the Justice assessment – police, courts and prisons. The investment in and depreciation of infrastructure associated with Justice services is carried out in the Investment assessment, using the recurrent assessment SDC disabilities, with adjustments for SDS.

Police Assessment

The police assessment is divided into two categories – specialised policing and community policing. The former recognises that there are certain police services which are a function of ‘demand’ for the services, incorporating population groups with a higher probability of committing crime while the latter consists of police services provided to the general community.

In the 2015 Review:

- The Commission applied judgement in splitting the expenses equally between the two categories.
- The SDC disability was applied to specialised policing, recognising that police spent more time and resources on some population groups than others. Three attributes were used to differentiate the population:
 - Age – People aged 0-14 and 65 or older were assumed to have negligible impact on specialised policing given their lower propensity to engage in criminal activity. Hence the age groups considered to be impacting the need for specialised policing were the groups aged 15-24, 25-44 and 45-64;
 - Indigeneity; and
 - SES measured using IRSEO and NISEIFA for the indigenous and the non-indigenous populations respectively.
- The age group data was measured using a 2007 national survey of people arrested and taken into custody by police while indigeneity and SES were measured using 2010-11 to 2012-13 State-provided data.
- Community policing need was assessed EPC since it is delivered for all residents and the need was considered to be independent of any law-breaking demographic drivers.

Wage costs, regional costs (measured using police-specific data) and service delivery scale were applied to the police assessment since those factors varied across the States and Territories and impacted assessed police expenses. Additionally, a National Capital factor was taken into account for the ACT recognising the higher than average wages that were paid to the AFP, noting that such an expense was beyond the control of the ACT Government.

Courts Assessment

The courts assessment is divided into two categories – civil courts and criminal courts.

In the 2015 Review:

- Assessed spending on courts was split 40:60 between civil and criminal courts based on the split published in the PC's ROGS.
- Civil court expenses were assessed EPC since there was no data indicating different rates of usage by different groups.
- Criminal court expenses were assessed using the same demographic groups as assessed in the police assessment, although the data sources were different.
 - Age profile was taken from ABS defendants data; and
 - Indigenous and SES profile were taken from data provided by four States and Territories for the period 2010-11 to 2012-13.
- Adjustments for Wage Costs, SDS and regional costs were also applied in the assessment, with impacts of some of the disabilities being further adjusted:
 - The SDS disability was applied to 50 per cent of court expenses since it was applicable for magistrates' courts only (higher courts are located in the major cities and regional centres); and
 - The regional cost disability used the regional cost gradient for police (as opposed to that of courts since such data was not available). Hence the assessed costs were discounted by 25 per cent to capture the uncertainty about the appropriateness of extrapolating data from police to courts.

Prisons Assessment

Assessed spending on corrective services focuses solely on the provision of prison services since they constitute the bulk (85 per cent) of the expenses in that component.

In the 2015 Review:

- Use of prison services was considered to have similar drivers as the police and courts assessments, i.e. different socio-economic and demographic populations.
- ABS data for adult prisoners and AIHW data for juvenile prisoners were used to measure usage by age and indigeneity. Effect of SES was taken from the measurement in the courts assessment.
- Adjustments due to wage costs and regional costs were also considered in the assessment. However, since the regional cost gradient from police data was used for prisons, similar to the courts assessment, the assessed expenses were discounted by 25 per cent to reflect the uncertainty about the appropriateness of extrapolating police data to prisons.

Overall, the Justice assessment redistributed \$976 million (\$39 pc) in the 2018 Update with \$47 million (\$112 pc) being redistributed away from the ACT.

Police Services

Context

The current assessment, based on the 2015 Review, applies a 50:50 split for expenses on community and specialised policing.

The 50:50 ratio was based on the Commission's judgement, since more specific data was not available on police resourcing. WA and the NT have expressed concerns citing that significantly more than 50 per cent of police resources in their jurisdictions are devoted to fighting and preventing crime, i.e. on specialised policing. States and Territories have also expressed concerns about out-of-date data since the assessment uses age data from a 2007 survey, a concern Commission staff also share.

Further, concerns have also been raised that offender numbers are not a good indicator for resource use since different types of offences involve different levels of resource use. Moreover, offender rates do not take into account other criminal-related services police provide that do not result in a person being taken into custody.

While Commission staff consider the current assessment to be relatively reliable, in the 2020 Review they are trying to develop a new assessment method which would address many of the concerns with the current one.

Elements of the proposed method, for which key model specifications have not been determined yet are:

- Assessed number of offences for a State or Territory is proposed to be determined using the same SDC factors as used currently – age, SES and indigeneity, along with remoteness. Commission staff especially note that indigeneity and SES are critical factors, since for example, indigenous offence rates are nine times that of the non-indigenous population.
- A cost per offence figure was calculated using police costs data at a station administration level and data on offences committed in each of the police administrative units.
 - It is worth noting that the use differentiators employed while calculating the **assessed number of offences** uses **data from offender location**, i.e. SES status of the offender and remoteness of the offender's residence. On the other hand, the cost differentiators employed in calculating the **cost per offence** is based on the attributes of where the offence is committed, i.e. SES and remoteness is **based on offence location**.
 - Analysis of the variation in cost per offence in NSW shows two distinct features:
 - Cost per offence increases with remoteness; and
 - Costs per offence in affluent suburbs of Sydney are very high, which Commission staff claim reflects both a level of community policing and relatively lower instances of crime.
- Commission staff have analysed cost per offence data from NSW, WA and the NT and their observations are as follows:
 - The proportion of indigenous persons in an area is inversely related to the cost per offence.
 - Cost per offence increases with remoteness.
 - Administrative areas with large populations have a lower cost per offence than those with small populations.

- Subject to variations due to remoteness and population size, the cost per indigenous offence is half the cost per non-indigenous offence, i.e. while the indigenous offence rate is nine times the non-indigenous offence rate, total police spending per capita for the indigenous population is only around 4.5 times the per capita spending on the non-indigenous population. However, Commission staff need data from other States and Territories to fully determine the relationship.
- Apart from developing an indigenous cost weight, Commission staff consider that a regional costs assessment can be developed from the data on increasing costs with remoteness and a SDS assessment can be developed from the relationship with population size.
- Hence, in summary, the Commission staff proposed approach consists of the following key steps and associated implications:
 - The use-based assessment developed using the SDC-based number of assessed offences is proposed to be adjusted using the cost per offence to accommodate different costs in different regional areas and for indigenous and non-indigenous offenders.
 - This approach removes the reliance on the judgement based 50:50 split between community and specialised policing that is used in the current assessment as the costs of community policing are already built into the model.
 - The proposed approach has the potential to capture the higher costs expended in policing certain types of crime, e.g. domestic violence, which are more prevalent in certain types of areas – although the influence cannot be identified separately.
- Since Commission staff have not fully analysed all State and Territory data yet, it is not clear whether the proposed approach will result in a reliable assessment.
 - If the proposed approach does not result in a reliable assessment, Commission staff intend to recommend to the Commission that the current approach should be continued, with minor modifications, including the removal of the 2007 custody survey data and sourcing of all socio-demographic data from a single source. Remoteness may also be added as a socio-demographic variable.

Commission Staff Position

Staff propose to recommend the Commission further develop a model incorporating socio-demographic drivers of offence numbers and geographic based drivers of cost per offence.

ACT Position

The ACT supports the Commission staff position of developing a model to determine the assessed expenses for policing. We note that it will remove the arbitrary 50:50 split between specialised and community policing that the current assessment entails.

One perspective that the ACT would like to share is with regard to the determination of assessed offences using offender location. An assumption inherent in this is that offender and offence locations will largely be in the same State or Territory. However, that may not be true when offender locations are in border areas.

In light of this, the ACT urges the Commission staff to also examine whether the total count of NSW-based offenders for criminal offences committed in the ACT is materially higher than the total count of ACT-based offenders for criminal offences committed in NSW, since it may mean that the number of assessed offences for the ACT has to be adjusted to take into account a cross-border disability. We intend to present the Commission with further information on this issue in a supplementary submission.

Courts

Context

The current assessment uses data from ROGS to estimate that 60 per cent of court expenses of \$1.5 billion can be attributed to criminal courts and extrapolates this percentage to the \$4.1 billion of spending on law courts and legal services identified in the GFS. The latter includes expenses for legal aid, public prosecution, crown solicitors and defenders, law reform commissions, anti-corruption agencies, public trustees, registrars, tribunals and licensing authorities, apart from criminal and civil courts.

Since prosecution and legal aid work primarily relates to criminal courts, Commission staff propose to assess these expenses using the same disabilities as for criminal courts. However, GFS data only identifies prosecution and legal aid expenses separately where those services are provided by separate agencies.

Commission staff estimate the 60 per cent expenditure on criminal courts in the following manner:

- Data for 2016-17 sourced from ROGS, in combination with other data on agencies supporting the criminal court system sourced from ABS GFS, show that direct expenditure on criminal courts represents 23 per cent of total State and Territory expenditure on legal services.
- GFS data shows that together with the criminal courts, other agencies' expenses are about 50 per cent of total legal services expenses. However, not all States and Territories have independent bodies providing legal aid and prosecution services, implying that their expense data is not captured separately in the GFS.
 - Without such expenses being captured, as shown in Table 7 (p. 11) of CGC 2018-01/16-S, legal aid accounts for 18 per cent of legal services' expenses and public prosecutions account for four per cent of such expenses.
- Assuming that States and Territories that do not have independent agencies spend a similar amount on a per capita basis as States and Territories that do, legal aid would increase to 20 per cent of all legal services expenses and public prosecution would increase to nine per cent of all legal services expenses. Hence, altogether, staff estimate that about 57 per cent of total law court and legal services expenses can be attributed to criminal courts and their supporting agencies.
- Hence, staff contend that the 60:40 split between criminal and civil courts implemented in the 2015 Review does not need to be changed.

Staff also propose to rename the 'courts component' to 'legal services component' as they consider that the latter better describes the range of services provided.

While Commission staff have observed substantial differences between the States and Territories in the number of finalisations per 100,000 people in civil courts, they have no information on whether such differences are driven by policy choices or disabilities. There is no data to support the latter as the SDC of civil court litigants and defendants are not collected.

Hence, continuing the method followed in the 2015 Review, Commission staff propose to assess civil court expenses on an EPC basis as far as use drivers are concerned. Similarly, for all other remaining elements of the legal cluster (Attorneys-General's offices, birth, deaths and marriage registrars, law reform commissions and tribunals), Commission staff propose an EPC assessment.

On the other hand, Commission staff propose to assess the use of criminal courts, legal aid and public prosecution services on a differential basis, similar to the 2015 Review. SDC comprising age, indigeneity and SES are the disabilities proposed. Staff propose to source all such data from the States and Territories every Census year.

The rates for each State and Territory would be calculated using State and Territory data every Census year and those rates would be applied to new annual State and Territory population data in the period between censuses. Since Census data may lead to a significant change to indigenous identification patterns, staff propose to send a new data request to States and Territories at that time, the first occasion being the 2021 Census.

As far as cost disabilities are concerned, Commission staff do not intend to recommend the Commission use cost-weight measures for the courts assessment. The primary reason is uncertainty of the available data. A summary of the approach the Commission staff pursued in this context is as follows.

- Commission staff attempted to differentiate between the cost of indigenous compared with non-indigenous defendants in the courts system.
 - Indigenous people are defendants in court at a higher per capita rate than non-indigenous people but this difference is greater in magistrates' courts than in higher courts. The cost per finalisation in the magistrates' court is one-twentieth of that in the higher courts. An examination of the use of such courts by the SDC characteristics of defendants, in tandem with the costs of those courts, enables the calculation of a cost weight for different socio-demographic groups across all criminal courts. Analysis of data from four States and Territories shows that a matter involving an indigenous person in the criminal court system costs 15 per cent less than for a non-indigenous defendant.
- However, for traffic and related offences, which make up almost 40 per cent of cases in the magistrate's court, very little data is available on the indigenous status of the defendants. Further only few traffic offences and only some situations related to traffic offences (e.g. refusal to pay fines) lead to court appearances.
 - If the assessment were to impute indigenous status using the assumption that the indigenous proportion of traffic and related magistrate's court defendants is the same as for all other offences, indigenous defendants for all courts would cost 10 per cent less than non-indigenous defendants on average. On the other hand, if indigenous persons were in court for these offences in the same proportion as their share of the total population, their average cost would be 20 per cent higher than their non-indigenous counterparts.

Hence, due to uncertainty in the available data, Commission staff do not intend to recommend the use of cost-weight measures in the assessment. They contend that the primary reason for such a scenario is the lack of data on indigeneity for traffic related court appearances.

Commission staff intend to contact the States and Territories on updated defendants' data, split between traffic and other offences, to update SES, age and indigeneity profiles. Staff intend to assess any available data on indigenous status of traffic and offence defendants before determining the most suitable treatment of these offences.

Commission Staff Position

Staff propose to recommend the Commission:

- Divide legal service expenses into those associated with criminal matters and all other legal services;
- Assess criminal legal matters using use rates based upon State and Territory data on the indigenous status, SES and age characteristics of criminal court defendants; and
- Not apply any cost-weights to population groups.

ACT Position

The ACT requests Commission staff to further investigate the proportion of criminal court and civil court expenses.

Data collected from the ACT's Justice and Community Safety Directorate indicate that expenses associated with legal aid for criminal related legal services accounted for just \$9.52 per capita in 2016-17 and not \$34 per capita as shown in Table 7 (p. 11) of the Draft Assessment Paper. Moreover, total legal aid expenses across criminal, civil and other legal services for the ACT were \$36.33 per capita in 2016-17, which is close to the \$34 per capita figure shown in Table 7. This raises the question whether the figures that have been used for legal aid are specific to criminal related legal services or apply to the entire legal services spectrum. Since these data are a key factor in the determination of the criminal to civil court expenses ratio, it is critical that any possibilities of error are rectified at the outset. As a matter of comparison, civil court expenses in the ACT were greater than criminal court expenses both in 2015-16 and 2016-17.

That said, the ACT supports the Commission staff recommendation on assessing criminal legal matters using use rates based on State and Territory data on indigenous status, SES and age characteristics of criminal court defendants. We also support the Commission staff recommendation on not applying cost-weights to population groups due to lack of data on indigeneity for traffic related court appearances.

As far as the scope of all legal services expenses is concerned, it seems that court processes associated with work done by anti-corruption agencies have not been identified under criminal or civil court expenses. We suggest that, since investigations by anti-corruption agencies are likely to lead to defendants being tried in criminal courts, expenses for anti-corruption agencies should also be considered under criminal court expenses.

Further, the ACT considers that including mention of the 'courts' in the name of this component of the justice services assessment would make its scope more intuitive.

Hence, the ACT suggests the name of this component should be 'courts and other legal services component' instead of the Commission staff suggested 'legal services component'.

Prisons

Context

The prisons assessment does not take into account non-custodial corrective services.

However, Commission staff consider that as reasonable since according to the 2018 ROGS, expenditure on prisons constitute 85 per cent of the net operating expenditure on corrective services.

Commission staff also consider that the current assessment captures the appropriate use and cost drivers, with high quality data for age and indigeneity drivers being available annually. However, data for SES drivers is less readily available and Commission staff propose to continue the 2015 approach of using the SES profile of criminal defendants as a proxy for that of prisoners. Although the data is available for only four States and Territories and requires data requests to the States and Territories for updating, Commission staff consider that it is still the best available source of SES drivers.

The SES data is sourced from States and Territories (using criminal defendants data) while age and indigeneity data are sourced from ABS and AIHW. Hence, the prisons assessment is based on a composite dataset. Staff contend that annual provision of new prisons data does not unduly add complexity to the assessment.

Commission Staff Position

Staff propose to recommend the Commission retain the 2015 Review method used to assess prisons.

ACT Position

The ACT broadly agrees with the Commission staff's proposition on drivers of use, but we do not consider the criminal defendants data from courts to be an accurate source of SES drivers for prisons.

Hence, similar to the method applied in the assessment of courts expenses, where the regional cost gradient for police is used as a proxy, we contend that this assessment should also be discounted by 25 per cent due to uncertainty about the appropriateness of using criminal defendants' SES data to measure SES of prisoners.

User Charges

Context

As per GFS figures, States and Territories raised \$1.6 billion in user charges in the justice sector (2015-16 figure), two-thirds of which was from the law courts and legal services component. The court charges were mostly related to civil courts rather than criminal courts and also included significant revenue from other legal services such as probate and registration systems. Revenue was also earned from cost recovery for services provided by police at special events – transport escorts, for control of traffic for film and television shoots etc. Staff consider that an EPC assessment is the most appropriate driver of all justice user charges.

Commission Staff Position

Staff propose to recommend that the Commission continues the 2015 Review approach of including justice user charges with Other Revenue.

ACT Position

The ACT understands that drivers of user charges are different from those for use of justice services and are also quite varied in nature. Hence, the ACT supports an EPC assessment of user charges. However, we consider that the user charges assessment should be presented in the Justice assessment since it improves the transparency of the assessment.

Other Issues

Commission Staff Position

Staff propose to recommend the Commission:

- Apply the Wage Costs assessment in the Justice assessment;
- Retain the 2015 Review method for regional costs and SDS; and
- Assess the influence of the use of AFP officers by the ACT on police expenses and fully incorporate it into the Justice assessment.

ACT Position

The ACT supports all the above Commission staff recommendations. We note that the ACT's use of AFP services was previously captured in the National Capital assessment and is now proposed to be captured in the Justice assessment. In view of our support for improving the transparency of specific assessments by incorporating related user charges in these assessments, the ACT supports this change too.

ROADS

Summary

The Roads assessment captures the recurrent costs associated with roads, bridges and tunnels. This includes the cost of traffic management, road safety programs, motor vehicle registration, driver licencing, heavy vehicle regulation and road transport planning administration.

The ACT is supportive of the proposed major methodology changes to base the Roads assessment on actual State and Territory road length data and to use lane-kilometres as the key indicator of road length as opposed to kilometres. This support extends to the use of actual road length data for local roads.

The ACT also supports the amalgamation of buses and rigid heavy trucks into a single category of heavy vehicles.

The ACT notes the Commission staff proposal not to investigate the relationship between urban density and road expenditure and recommends that the Commission staff reconsider their position.

The ACT supports the Commission staff efforts to develop a data-based factor for bridges and tunnels, but considers that if Commission staff are unable to develop a model to differentially assess bridge and tunnel needs, these expenses should continue to be assessed on an EPC basis as in the 2015 Review methodology.

The ACT does not support the Commission staff proposal to remove the other services component from the Roads assessment and distribute the expenditure proportionally between the remaining components. The ACT considers that other services should continue to be assessed on an EPC basis as in the 2015 Review methodology.

The ACT does not support the ongoing discounting of NNRO Commonwealth payments and considers that these payments should be fully equalised.

While the ACT is supportive of road user charges continuing to be assessed on an EPC basis, we do not support the Commission staff proposal to continue to assess road user charges under the Other Revenue assessment. The ACT considers that the revenues captured in the Other Revenue assessment should be minimised in order to maximise the transparency of assessments.

The ACT supports the ongoing application of regional and wage cost loadings to the Roads assessment, in acknowledgement that States with more remote communities and higher wages face greater service provision costs than States with less remote communities and lower wages. The ACT also acknowledges the difficulty in developing a road maintenance expenditure assessment on the basis of the physical environment and supports the Commission staff proposal not to pursue this further.

Context

The Roads assessment captures the recurrent costs associated with roads, bridges and tunnels.

This includes the cost of traffic management, road safety programs, motor vehicle registration, driver licensing, heavy vehicle regulation and road transport planning administration.

Under the 2015 Review methodology, the Roads assessment is broken into five components:

- Rural roads;
- Urban roads;
- Local roads;
- Bridges; and
- Other services.

In the provision of roads, States and Territories are assessed on the length of their road networks, traffic volume and heavy vehicle use. Road length is assessed separately for rural and urban roads, with road length for rural roads calculated based on a synthetic network. The synthetic network indicates the required length of road to connect localities of 400 or more people using the fastest possible route.

Urban road length is assessed on each State and Territory's population residing in urban centres with more than 40,000 people. The 40,000 threshold was chosen to align with the ABS definition of urban centres in the *Survey of Motor Vehicle Use*. Finally, local road lengths are determined on the basis of the length of minor roads in remote and very remote regions with populations of less than one per 100 km². The length of rural roads used was measured in a consultancy prior to the release of the 2015 Review report.

Traffic volume is also assessed separately for rural and urban roads on the basis of vehicle kilometres travelled, obtained from BITRE. The BITRE dataset in turn is based on the ABS Survey of Motor Vehicle Use.

Heavy vehicle use is also assessed separately for rural and urban roads and is calculated based on the average gross mass of different classes of vehicles by the vehicle kilometres travelled in each State and Territory. Bridges and other services are assessed on an EPC basis.

The Roads assessment redistributed \$46 million, or \$110 per capita in GST funding from the ACT in the 2018 Update.

Commission Staff Position

Commission staff, in Draft Assessment Paper 2018-01/17-S, have proposed significant changes to the Roads assessment. Chief among the proposed changes is to replace the current synthetic network and urban centre methodology for assessing road length with an assessment methodology using actual State and Territory road length data from State and Territory geospatial datasets on their road networks.

State and Territory actual road lengths would be adjusted to only capture roads that are commonly classified among jurisdictions as State or Territory roads and for other average policy considerations, such as the number of connections between population centres or areas of significance.

The adjusted actual road lengths would further be split between urban and rural roads, with urban roads being defined as roads within urban areas of more than 40,000 people as in the 2015 Review methodology.

Another proposed major change is to calculate road lengths in terms of lane-kilometres rather than just kilometres as in the 2015 Review methodology. Commission staff argue that this change would capture the additional costs incurred by States and Territories for providing above-average levels of multi-lane roads. Commission staff note that data on lane-kilometres is not readily available and would need to be estimated. Commission staff have indicated that State and Territory road authorities may be required to assist in developing estimates of lane-kilometres and they would ideally be consistent with the still-under-development Austroads Standard.

Commission staff further propose to extend the use of actual State and Territory data to the local roads component as well, using actual State and Territory road length data to update its estimates of local road length. Commission staff further propose to ensure that ongoing rigour is applied in the local roads component by only including expenses relating to the maintenance of roads in unincorporated areas or areas with insufficient populations for local government to be able to support their maintenance.

Commission staff propose to retain the 2015 Review methodology for calculating urban and rural traffic volume, however they propose two minor adjustments to the assessment of heavy vehicle usage. Commission staff propose to exclude light commercial vehicles from the heavy vehicles classification, which Commission staff argue would be consistent with Australian Heavy Vehicle Law.

Further, Commission staff propose to simplify the assessment by reducing the number of heavy vehicle categories through combining rigid and other trucks with buses.

Commission staff have also responded to comments made by the ACT in our response to the Commission Staff Research Paper *What States Do – Roads* regarding the effect of urban population density. The ACT indicated that States and Territories with higher urban area per capita (i.e. lower urban density) spend more per capita on roads than States and Territories with lower urban area per capita (i.e. higher urban density). The ACT suggested that the Commission should investigate this as a possible adjustment to the Roads assessment. Commission staff consider that the relationship between roads expenditure per capita and urban density is not strong and have proposed that the matter not be pursued.

Commission staff have indicated an interest in pursuing a bridge and tunnel factor based on State and Territory spatial data on topography, road network size and traffic volume. However, Commission staff have indicated that if a reliable measure of bridge and tunnel needs cannot be developed, they will propose that relevant bridge and tunnel expenses and investment will be incorporated into the urban and rural roads components and subject them to the same disabilities.

Commission staff have also proposed to remove the other services component from the Roads assessment and reallocate related expenses to the other components of the assessment on a proportional basis.

Commission staff have indicated that this would make the treatment of other services in the Roads assessment consistent with their treatment in State and Territory financial statements.

Commission staff have deferred a decision on possible changes to the treatment NNRO and NNRA projects and seek State and Territory views on whether the Commission should continue to discount 50 per cent (or another proportion) of Commonwealth Government payments to States and Territories for NNROs or if these grants should have no impact on the GST distribution.

Commission staff have also proposed to continue to apply wage cost and regional cost factors to the Roads assessment and to continue to assess roads user charges on an EPC basis in the other revenue assessment. Commission staff have also noted that attempts to develop a physical environment assessment for road maintenance expenditure have been difficult in the past and have proposed to not pursue such an assessment in the 2020 Review.

ACT Position

The ACT supports the proposed major methodology change to base the Roads assessment on actual State and Territory road length data. This support extends to the use of actual road length data for urban, rural and local roads. The ACT considers that this proposed approach is more consistent with the principle of *What States Do* than the 2015 Review's synthetic network approach and will more accurately capture the extent of State and Territory road networks, provided appropriate adjustments are made for State and Territory policy differences.

In relation to local roads, the ACT also supports the Commission proposal to limit the scope of local roads captured in the assessment to roads in unincorporated or sparsely populated areas. The ACT considers that this restriction would minimise the contamination of the assessment with local government services while still maintaining policy neutrality.

The ACT does acknowledge that there is a risk of compromising the principle of *Policy Neutrality* by using State and Territory data, through discrepancies in the classification of roads in different jurisdictions as State/Territory or local roads. This issue has also been identified by Commission staff. However, like the Commission staff, the ACT considers that this risk would be mitigated through the use of common classifications. We note that the Commission has identified the proposed Austroads Standard and support further investigation into its use as the common classification for the comparison of State and Territory road data. The ACT is able to provide road data, including location, class, length, width, the number of lanes and lane-kilometres on the basis of the Austroads Standard.

The ACT is also supportive of the Commission staff proposal to use lane-kilometres as the key indicator of road length as opposed to kilometres. Noting that the number of lanes in a given road is a significant driver of the cost to both build and maintain it, the ACT considers that the proposed approach would more accurately capture the cost to States and Territories of providing roads given their needs.

The ACT supports the Commission staff proposal to merge buses and rigid heavy trucks as a simplification measure. We note that there is no evidence that buses and rigid heavy trucks cause differing levels of wear on roads and thus consider that there is no conceptual basis for maintaining the split.

Regarding the relationship between urban density and road expenditure, the ACT notes the Commission staff proposal not to investigate this relationship further on the basis of the weakness of the correlation between urban density and roads expenditure in the 2015 data shown in the Commission Staff Research Paper *What States Do - Roads*.

While we acknowledge that the 2015 data does not show a definitive relationship between urban density and roads expenditure, the ACT recommends that Commission staff reconsider their position and investigate the relationship further.

The ACT supports the Commission staff efforts to develop a data-based factor for bridges and tunnels. We note that bridges and tunnels are generally only used to traverse obstacles that cannot be avoided or removed, such as major watercourses and valleys. Bridges and tunnels are both very expensive to build and maintain and their use is avoided whenever possible.

However, if Commission staff are unable to develop a model to differentially assess bridge and tunnel needs, the ACT would not support these expenses being incorporated into the road length assessment and thus subject to the same assessment methodology. The ACT considers that the primary drivers of road length are the number and size of population centres and other locations of significance within a State or Territory and the distance between them. Whereas, as indicated earlier, bridge and tunnel needs are primarily driven by the prevalence of unavoidable obstacles. Given these differences in cost drivers, the ACT considers that if Commission staff are unable to develop a model to differentially assess bridge and tunnel needs, these expenses should continue to be assessed on an EPC basis as in the 2015 Review methodology.

Further, the ACT does not support the Commission staff proposal to remove the other services component from the Roads assessment and distribute the expenditure proportionally between the remaining components. The ACT considers that many of the services captured in the other services component, such as road safety programs, heavy vehicle regulation and road transport planning administration have significantly different cost drivers to those that drive the provision and maintenance of roads and road assets. These services are largely administrative in nature and are provided regardless of road network size, effectively amounting to Administrative Scale costs.

Moreover, expenditure on services such as road safety programs are primarily driven by factors not considered by the Commission in the other components, such as the number of road fatalities or the prevalence of drunk driving. The ACT considers that other services should continue to be assessed on an EPC basis and does not consider the appearance of such expenditure in State and Territory financial statements to be a relevant consideration for equalisation purposes.

The ACT does not support the Commission's current discounting of Commonwealth payments for NNROs by 50 per cent and considers that all Commonwealth payments for NNROs should be fully equalised with no discounting. Our position on this issue is further elaborated upon in the Commonwealth Payments chapter of the submission.

The ACT does not support the Commission staff proposal to continue to assess Road user charges under the Other Revenue assessment. As previously indicated, the ACT considers that all user charges should be captured in their relevant assessments and that the revenues captured in the other revenue assessment should be minimised. We consider that this approach is the most transparent method of categorising user charging revenues.

However, the ACT supports the ongoing assessment of road user charges on an EPC basis. As identified by the Commission, the ACT considers that the drivers for revenue raising capacity from roads user charges are not the same as those used to assess the other road factors.

We agree with the Commission that an EPC assessment is the most appropriate method of assessing road user charges.

That said, the ACT is cognisant of the ongoing efforts on Roads user charging reform being undertaken, particularly in regard to heavy vehicles through the Heavy Vehicle Road Reform program. The results of Roads user charge reform may more closely align Roads user charges with State and Territory expenditure needs, which would give credence to netting Roads user charge revenue off Roads expenditure. The ACT considers that the Commission should monitor this area closely as the 2020 Review is progressed.

The ACT supports the ongoing application of regional and wage cost loadings to the Roads assessment, in acknowledgement that States and Territories with more remote communities and higher wages face greater service provision costs than States and Territories with less remote communities and lower wages. The ACT also acknowledges the difficulty in developing a physical environment disability for road maintenance and supports the Commission staff proposal not to pursue this further.

TRANSPORT

Summary

The Transport assessment consists of assessments of net recurrent expenses for Transport while infrastructure investments in Transport are assessed in the Investment assessment. The Draft Assessment Paper on Transport covers the assessments of both recurrent expenses and infrastructure investments.

- The ACT does not agree with the Commission staff proposal to retain the current general approach to the assessment of recurrent and infrastructure expenditure on urban transport. Key reasons are:
 - The use of regression models with only a few observations, as Commission staff themselves comment in the Staff Research Paper *A Broader Assessment Approach*, is prone to producing results where the models not only capture the underlying needs but also the impact of factors correlated to above average effort.
 - The ACT disagrees with population being the only driver for net urban transport expenses and investment in infrastructure.
- The ACT agrees with the Commission staff proposal to provide the report on Stage Two of the consultancy to the States and Territories for comments and the plan for Commission staff to develop assessment proposals for net expenses and transport infrastructure investments for the Commission after receiving those comments.
- We agree with all the Commission staff recommendations on the definition of urban areas, inclusion of all SUAs in the assessment of urban transport and the criteria on which decisions to amalgamate satellite cities with their principal city should be based.
- The ACT does not support the Commission staff recommendation to retain the 2015 Review assessment of non-urban transport services, based on State and Territory shares of population outside capital cities and recommends investigating the impact of other potential drivers such as geography and topography.

Context

The Commission staff Draft Assessment Paper on Transport CGC 2018-01/18-S encompasses the assessments of transport net expenses and investment. The former is assessed in the Transport assessment while the latter is assessed in the Investment assessment.

State and Territory expenses related to bus, rail (passenger and freight) and ferry services, ports and other maritime related services and air transport are included in the Transport assessment. Further, expenses for passenger concessions and State and Territory administration expenses are also included while any user charges or other sources of revenue are netted off from the total expenses.

The transport investment component comprises investments in the acquisition of additional or upgraded infrastructure, with investment being defined as gross capital expenditure less depreciation.

Two components constitute the Transport assessment, namely urban transport net operating expenses and non-urban transport subsidies.

States and Territories expended \$13.5 billion on Transport in 2016-17, with \$12.5 billion being the net operating expense on urban transport and \$1 billion being the expense on non-urban transport subsidies. States' and Territories' investment in transport infrastructure was \$7.8 billion in 2016-17.

The conceptual case on which the assessment of net urban transport operating expenses rests is that, even after taking into account fares and other revenue, State and Territory governments spend more per capita in larger cities than in smaller ones.

Analysis of per capita net expenses from 2009-10 to 2011-12 according to populations of cities shows that, in comparison to per capita net expense incurred in cities with population between 250,000 and one million:

- Per capita net expenses were 71 per cent higher in cities with population between one million and 2.5 million (\$321 pc versus \$188 pc); and
- Per capita net expenses were 126 per cent higher in cities with population of 2.5 million and above (\$426 pc versus \$188 pc).

Transport consultants engaged for the 2010 Review had also advised that the quantity of travel by public transport, measured in passenger-kilometres, rose even faster in growing urban centres as the average trip distance increased with growth in urban areas. Hence, the Commission considered population size to be an appropriate representation for the transport task in the 2010 and 2015 Reviews.

Analysis of per capita net expenses and per capita travel by public transport (measured in passenger-kilometres) also shows a similar trend as per capita net expense tends to increase with increase in the per capita passenger-kilometres travelled, supporting the conceptual case presented above.

In the 2015 Review, the Commission used consolidated general government sector and PNFC expenditure and investment on urban passenger transport services, since it considered transport services to be more like general government services than the commercial services provided by many State and Territory trading enterprises.

The decision was on the grounds that, like general government agencies, for urban transport services the policies on service delivery and charges are decided by government departments, the services originate from social policy objectives and both general government agencies and urban transport enterprises rely on the government for funds to meet operating costs and major investments.

Since the Commission considered population size to be an appropriate proxy for the transport task in the 2015 Review, the following model was used for the assessment of urban transport net expenses.

$$E_i = \beta * \ln(P_i) + \alpha$$

Where:

i denoted all cities with population greater than 20,000;

E_i denoted the per capita net expense for city i ;

P_i denoted the population of city i (in millions);

α was a constant (equal to per capita net expense in a city with a population of one million);

β was a scaling factor.

Based on data shared by State and Territory transport departments in the 2015 Review data returns, the above model was estimated as net operating expenses, $E = 90.17 * \ln(P) + 291.29$.

The urban centres which were considered to be in scope were ABS UCLs contained within SUAs, urban centres with populations above 20,000 were included. The Commission considered Newcastle, Wollongong, the Central Coast, Sunshine Coast and the Gold Coast as separate cities, instead of amalgamating them with their principal cities (Sydney and Brisbane, as applicable). The rationale was that demand for public transport between these satellite cities and the principal city was low relative to public transport travel within the satellite city. This approach was supported by the 2010 Review consultants.

The other component in the Transport assessment is the non-urban subsidies, which covers the cost of providing passenger and freight transport services between urban centres. In the 2015 Review, needs were measured by each State and Territory's share of its population living outside capital cities. Wage Costs and regional costs were applied as disabilities to determine the final assessed expense for non-urban subsidies.

The urban transport investment assessment was carried out in the Investment assessment in the 2015 Review. It took into account the factors affecting investment in transport infrastructure:

- City size, taken into account through a capital stock factor, calculated as an average of factors derived from:
 - A **population model** reflecting the effect of city size on the need for assets per capita; and
 - State and Territory shares of people residing in urban centres with population above 20,000.
- Population growth; and
- The cost of urban transport infrastructure, taken into account through a capital cost factor reflecting the relative construction, wage and regional costs.

The **population model** used to determine the capital stock factor was based on the Commission's analysis which showed that assessed asset values per capita were driven by the square of urban centre populations if the relationship between city size and asset values was linear and had a zero intercept (i.e. passed through the origin). The simplified model that the Commission adopted was as follows:

$$A_i = P^2 * 0.5$$

Where:

i denoted all cities with population above 20,000;

A denoted assets per capita;

P denoted urban population; and

0.5 was the discount on the assessment.

Depreciation expenses were included in the assessment of net urban transport operating expenses.

The non-urban transport investment assessment recognised the impacts of service use and interstate differences in population growth on the relative need for infrastructure acquisition and maintenance. Differences in cost of infrastructure across States and Territories was also taken into account. Depreciation expenses pertaining to non-urban transport investment were assessed in the Depreciation assessment.

In the 2018 Update, the transport net recurrent expenses assessment redistributed \$888 million, with \$70 million being redistributed away from the ACT. The urban transport component in the Investment assessment redistributed \$793 million, with \$25 million being redistributed away from the ACT.

Conceptual Case

Context

For the 2020 Review, the Commission has engaged a consultant who is working with the Commission staff to identify the drivers of State and Territory urban transport expenses. The latter acknowledge that there is no Australian or international literature which directly addresses the question of the factors that drive **net** urban transport operational expenses. Existing literature considers each of the factors separately – the demand for, supply of and costs of transport services.

Hence, in CGC 2018-01/18-S, Commission staff proceed with discussions on factors that affect demand, supply and costs of public transport, classifying them into policy and non-policy influences. They summarise their approach stating that the non-policy influences can be classified into two groups: population size and characteristics, and urban form and topography, and reiterate that the 2015 Review recurrent expense and infrastructure models recognise the impact of population size on urban transport expenses.

Further, Commission staff propose to not adjust data for Sydney and Melbourne either because of policy influences or because of significant effects on the results, since it would move the assessment away from *What States Do* and would be inconsistent with the Commission's other assessments. They cite the example of the Commission's assessments of remoteness in this regard.

Commission staff also cite data from Spain, France and the USA to show that broadly, per capita subsidies do increase with city size.

Commission Staff Position

Staff propose to recommend the Commission retain the current general approach to the assessment of recurrent and infrastructure urban transport expenditure because the conceptual case that city population is a major driver of net expenses and assets for public transport systems is strong and supported by data.

ACT Position

The ACT does not agree with the Commission staff position. We do not consider that the position on the 'conceptual case' can be considered separately from the recommendation on the modelling of transport expenses and transport investment as part of stage 2 of the work to be carried out by the consultants. In our view the two go together and treating them separately is akin to overlooking that the crux of the assessment methodology is dependent on the regression models, which in turn are heavily dependent on the conceptual case.

In Commission Staff Research Paper CGC-2018-02-S *A Broader Assessment Approach*, Commission staff cite that a significant challenge with regard to using regression analysis of the drivers of transport costs is the small number of data points involved (para 69, p. 17). They acknowledge that with only eight States and Territories, a regression to predict actual costs will not only identify the underlying drivers of expense need, it will also include the impact of factors correlated with above average effort. Further, the option of increasing data points by using data for more than one year is ruled out since it would need State and Territory demographic attributes and spending data to be independent year-on-year whereas such variables are observed to change slowly over time, i.e. the year-on-year data are highly correlated.

The ACT agrees with those comments and considers that it would be worthwhile to get some understanding of how useful the regression models for transport recurrent expenses and investment in transport infrastructure really are. In view of that, we would appreciate if Commission staff can share the details of the error variance of the model and Cook's distance¹⁴ values for the data for Sydney and Melbourne associated with the regression model that was used in the 2015 Review and the regression model that is proposed to be used for the 2020 Review, once it is developed.

The stage one report provided by the consultant on the modelling of net transport expenses and investment in transport infrastructure, which the ACT found to be quite insightful, clearly shows that city size/population, while being important, is not the only driver of transport expenditure. Hence, we consider that it is not accurate to maintain the position that the conceptual case still continues to hold, with population as the **only** driver of net expenses and assets for public transport systems. We observe that Commission staff use the term **major driver** for population in the above recommendation while in reality, the models used in the 2015 Review considered population to be the **only** driver. At the same time, the ACT acknowledges that adding more independent variables to the regression model without any change in the number of observations has the possibility of increasing the error variance and impacting the usefulness of the regression model. Hence, conclusions on the utility of the regression model approach can only be drawn after an initial model has been developed and its characteristics analysed.

Further, while the ACT appreciates the case for Commission staff not altering data for cities, in our view the comparison of influence of data for cities like Sydney and Melbourne on the transport assessment with the influence exerted by data from QLD, WA and the NT on the remoteness assessment is not accurate. For the remoteness assessment, data is available well below the whole-of-State/Territory level, i.e. at a fairly granular level.

¹⁴ Cook's distance is useful for identifying outliers in the X values (observations for predictor variables). It also shows the influence of each observation on the fitted response values. An observation with Cook's distance larger than three times the mean Cook's distance might be an outlier. (Source: <https://au.mathworks.com/help/stats/cooks-distance.html>)

However, that is not the case for the transport assessment where Sydney and Melbourne are two data points exerting extreme influence on the results.

Urban Transport Expenses and Infrastructure Models

Context

As a part of the 2020 Review, the Commission has engaged a consultant with transport economics expertise to:

- Develop a model or models that can be used to assess States' and Territories' recurrent urban transport and transport infrastructure expenses; and
- Provide confidence to States and Territories that the model(s) and data used are reliable and fit for purpose.

This is because, as mentioned earlier, the States and Territories had expressed concerns about the models used in assessing net urban transport expenses and infrastructure requirements on the following grounds:

- Use of population as the **sole** driver of net urban operating expenses; and
- Appropriate shape of the relationship between population and per capita expenses and asset values.

Commission staff have shared the stage one report prepared by the consultant with the States and Territories. In stage two, the consultant is exploring whether current models can be improved by including non-policy factors like population characteristics, urban form and topography.

Commission staff have collected data on urban transport expenditure, assets and use from the States and Territories and shared that with the consultant to aid in that modelling exercise. Commission staff intend to share the stage two report with the States and Territories for comments once the consultancy is complete. After receiving comments from the States and Territories, Commission staff will develop assessment proposals for net urban transport expenses and infrastructure investment for the Commission. If the consultant is unable to develop simple and intuitive models that are able to capture State and Territory needs better than the current ones, Commission staff intend to propose that the current approach be retained and update the assessment with recently collected data.

Commission Staff Position

Commission staff propose to provide the report on stage two of the consultancy to the States and Territories for comments. After receiving those comments, staff will develop assessment proposals for net expenses and investment for the Commission.

ACT Position

Given the ACT's position on the 'conceptual case', the ACT agrees with the Commission staff position expressed here. We reiterate that the previous proposition and this one should ideally be considered together since the regression models are based upon the conceptual case.

Definition of Urban Areas

Context

Commission staff propose to retain the 2015 Review definition of urban areas, ABS UCLs contained within SUAs, which was supported by the consultant in its stage one report, with one change. In the 2015 Review, only SUAs with population above 20,000 were included while for the 2020 Review staff propose to include all SUAs. This would increase the number of urban areas from 65 to 106. Commission staff consider that it will better reflect *What States Do*.

Commission staff had asked the consultant to review which satellite cities could be amalgamated with the principal city in view of QLD's argument to that effect on amalgamating Gold Coast with Brisbane after the 2015 Review. The consultant has proposed the following two criteria to determine whether satellite cities should be amalgamated with the principal city.

- A threshold indicating maximum travel time of 120 minutes between the principal and satellite cities by public transport during morning peak hours; and
- The proportion of inter-city commute trips is greater than five per cent of satellite intra-city commute trips, indicating some level of labour market integration between the principal and satellite cities.

Analysis based on the above criteria will form a part of the stage two report, though some examples were shared in the stage one report, indicating that the Gold Coast could possibly be considered as a satellite city of Brisbane.

Commission Staff Position

Staff propose to recommend the Commission:

- Retain the 2015 Review definition of urban areas: ABS UCLs contained within SUAs;
- Include all SUAs in the assessment of urban transport because most of them have public transport services; and
- Decide whether or not some satellite cities should be amalgamated with their principal city based on the results of the analysis using the two quantitative criteria proposed by the consultant.

ACT Position

The ACT agrees with the Commission staff recommendation on all the above points. That said, the ACT notes ABS advice that SUAs *"can include related peri-urban and satellite development and the area into which the Urban development is likely to expand"*, implying that the choice of SUAs will lead to some of the satellite cities being merged into the principal city.

Advice provided by our Transport Canberra and City Services Directorate in relation to Queanbeyan is that public transport travel time between Canberra (city centre) and Queanbeyan averages 45 minutes, with 41% of work trips from the Queanbeyan district being made to the ACT and only 20% of these trips being made within the Queanbeyan district (based on 2016 ABS Census data). These data indicate that Queanbeyan can be considered a satellite city of Canberra.

Non-urban Expenses

Context

Commission staff propose to retain the 2015 Review assessment of non-urban transport services, which was based on State and Territory shares of population outside capital cities. Commission staff contend that the States and Territories had supported the approach in the 2015 Review.

Commission Staff Position

Staff propose to recommend the Commission retain the 2015 Review assessment of non-urban transport services.

ACT Position

The ACT does not support the Commission staff recommendation. Apart from population outside capital cities, factors like State and Territory geography and topography, the population distribution across the non-urban centres and their relative distances from main urban centres can also exert significant influence on non-urban transport expenses. The ACT requests Commission staff to examine the impact of such factors on the assessment.

SERVICES TO INDUSTRY

Summary

The Services to Industry assessment captures expenditure on the regulation and development of industry and other economic affairs, such as registration, licensing, occupation health and safety and employment conditions.

The ACT is generally supportive of the Commission staff proposals for the Services to Industry assessment, including the ongoing assessment of business development expenses on an EPC basis, the ongoing differential assessment of regulation expenses and the collection of data for updating major infrastructure project planning cost estimates.

Regarding R&D expenses, the ACT considers that a consistent approach should be applied to the treatment of all R&D expenses. If they are not driven by the factors relevant to the separate expense categories, then it makes sense to bring them together in the one assessment, once the new GFS classification is available to identify the expenditure.

Further, the ACT supports the updating of administrative scale costs for Services to Industry. We have outlined our position on administrative scale further in the Administrative Scale chapter.

The ACT also supports the Commission staff proposals on Services to Industry user charges. The ACT's position on user charges more generally is set out in the Other Revenue chapter.

Context

The Services to Industry assessment covers State and Territory spending on the regulation and development of businesses and industries and other economic affairs. Some spending relates to specific industries including agriculture, forestry, mining, manufacturing, tourism and construction. Other spending relates to all businesses, or to consumers.

- Examples of regulatory functions include business registration, licensing of tradespeople, livestock identification schemes, chemical and pesticide regulation, building codes, energy market regulation, product safety, occupational health and safety, consumer protection, mine safety, employment conditions and shop trading hours.
- Examples of business development activities include mineral exploration, geological mapping, agricultural irrigation systems, tourism and trade promotion, marketing and industry research and development.

Services to industry net expenses were \$6.2 billion in 2016-17.

Regulatory expenses are assessed differentially, based on type of industry and State and Territory shares of production and construction. Agriculture is assessed separately from other industries, reflecting the different approach and higher costs of regulation in this sector, in particular due to the food safety and biosecurity arrangements which apply to agriculture.

Business development expenses are assessed EPC, with adjustments for Wage Costs and administrative scale. An EPC assessment is applied because the Commission could not identify the conceptual case for a differential assessment.

User charges for mining regulation are deducted from mining expenses before making the assessment but other user charges are assessed EPC in the Other Revenue assessment.

The Services to Industry assessment redistributed \$15 million, or \$36 per capita in GST revenue from the ACT in the 2018 Update.

Business Development Expenses

Context

Business development expenses are defined as State and Territory expenses (grants, subsidies or government services) intended to assist or benefit businesses or industry. Examples include:

- Research and development;
- Rural irrigation projects;
- Trade and investment promotion;
- Tourism and major events development and promotion;
- Small business support;
- Drought assistance;
- Regional economic development;
- Job creation measures;
- Mining exploration and geological surveying; and
- Other industry assistance.

Commission Staff Position

In the 2015 Review, the Commission assessed business development expenses EPC because it could not identify the conceptual case for a differential assessment and population seemed to be the most appropriate driver. It was unable to establish why a State or Territory would need to spend more or less than the average in developing its industries and businesses. All States and Territories fund business development, but States and Territories exercise considerable discretion in deciding how much to spend and which industries should benefit.

However, Wage Costs and Administrative Scale disabilities are applied to business development expenses to reflect input cost differences between the States and Territories.

Staff propose to recommend the Commission:

- Continue to assess business development expenses EPC;
- Continue to apply the Wage Costs disability to State and Territory business development expenses; and
- Continue to recognise that there are minimum fixed costs associated with the normal range of business development activities States and Territories perform.

ACT Position

The ACT supports the Commission staff proposals.

We consider that State and Territory governments all pursue policies which they consider favourable to the economic development of their State/Territory, but the emphasis of these policies will depend on natural endowments, demographic characteristics and historic settlement factors specific to each of them. Hence, generic quantifiable drivers of expenses are difficult to identify. We do note however that the Physical and Financial Assets assessment differentially assesses State and Territory expenditure on economic infrastructure such as roads and transport, with population growth as the major driver. This at least partly accounts for State and Territory economic development needs.

The ACT also considers that further consideration should be given to the impact of direct Commonwealth assistance to industry on State and Territory business development needs. We will examine provision of additional information on this issue as part of a supplementary submission.

Regulation and Other Industry Support Services

Context

Regulation includes development and enforcement of guidelines, codes, standards, rules or laws designed to control, govern or influence the way people and businesses behave. Most of the regulation expenses included in this category relate to businesses and industry. Regulation of other sectors, such as education or health, is included in the relevant expense assessment.

Other industry support services are those which are not strictly regulation or business development. Examples include biosecurity responses and drought preparedness.

Commission Staff Position

The Commission considers the broad driver of regulatory costs is the size of each regulated industry, as measured by value of production or number of businesses.

Data are not available from the GFS which discriminate between business development and regulation expenses by industry sector. Hence, the Commission relies on a State and Territory data collection to estimate these expenses. However, data on R&D expenses for all industries are available from the GFS.

Commission staff are proposing a narrowing of the approach to business development expenses which will assume that all expenses other than for specifically defined purposes relate to regulation activities.

Staff propose to recommend the Commission:

- Use State and Territory data on business development expenses and GFS data to estimate business development and regulation expenses for agriculture and other industries;
- Continue to assess agriculture and other industries regulation separately because the way States and Territories regulate these sectors is different, but only if a separate agriculture assessment remains material;

- Send draft data requests for agriculture and other industries in May 2018;
- Send final data requests to the States and Territories in September 2018 to collect the final data for three financial years from 2015-16 to 2017-18; and
- Retain the business development and regulation weights obtained from data for 2015-16 to 2017-18 for the period of the 2020 Review.

In relation to the drivers of regulation expenses, staff propose to recommend the Commission:

- Continue to differentially assess industry regulation expenses because the size of the regulation task for industry is related to the size of the sector; and
- Use information from State and Territory line agencies to inform the decision on the relevant drivers of State and Territory spending on industry regulation.

Commission staff considered a proposal from WA to use a regression approach to identify and weight the drivers of agricultural expenses. However, staff proposed this approach be rejected because data were not available to split regulation from business development expenses and the regression result also appeared to be substantially influenced by policy differences.

ACT Position

The ACT supports the staff proposals.

Planning and Regulation for Major Infrastructure Projects

Context

The 2015 Review introduced an assessment of State and Territory spending on planning and regulation for major infrastructure projects. The Commission considered that States and Territories with higher levels of private sector investment incur higher planning and regulation costs. State and Territory shares of private non-dwelling construction expenditure were used as the driver of assessed differences between States and Territories.

Commission Staff Position

Staff propose to recommend the Commission:

- Continue to assess planning and regulation expenses for major infrastructure projects in the Services to Industry assessment using State and Territory shares of private non-dwelling construction expenditure as the disability; and
- Collect data from States and Territories to update the current spending estimate.

ACT Position

The ACT supports collection of data to update the current spending estimate. However, we propose that the driver of planning and regulation costs for major infrastructure projects be driven by non-State/Territory non-dwelling construction, rather than just private non-dwelling construction.

We propose this expansion in light of the special characteristics of the ACT economy as expanded upon in Part C of this submission, wherein the public sector, through the Commonwealth government, drives a far larger proportion of the ACT's economic activity than it does in the States and the NT. We consider that expanding the driver to include all non-State/Territory non-dwelling construction would alleviate this concern, as well as more accurately capture the scope of ongoing major infrastructure development in each State and Territory in general. We also note that the proposed expansion would still exclude State/Territory non-dwelling construction and thus would face no additional concerns in regard to *Policy Neutrality*.

Other Research and Development Expenses

Context

Industry R&D expenses are currently assessed EPC in this assessment, though some R&D spending is included in other expense assessments and assessed using the relevant disabilities for the assessment. The current GFS does not separately identify research and development spending by industry sector, but these splits will be available in the new COFOG-A classification.

Commission Staff Position

Staff propose to test the materiality of applying assessment disabilities to R&D spending and, if material, transfer the expenses to the Services to Industry assessment, to be assessed EPC. The implicit assumption is that R&D expenditure is not driven by the factors which influence service delivery type expenses and, in the absence of a clearly identifiable driver, should be assessed EPC. This would also bring together all R&D expenses in a single assessment.

ACT Position

The ACT considers that a consistent approach should be applied to the treatment of all R&D expenses. If they are not driven by the factors relevant to the separate expense assessments, then it makes sense to bring them together in the one assessment, once the new GFS classification is available to identify the expenditure.

User Charges

Context

Commission staff consider that most of the revenue in this assessment relates to regulation rather than business development (e.g. agricultural levies). States and Territories assessed as having higher regulation costs will also have a greater capacity to raise revenue through fees and charges. This means that netting the user charges off expenses and assessing the net expenses is equitable, as well as being the simplest approach. The current assessment nets off user charges for regulatory functions only from mining related regulatory expenses. The latter represent only about 10 per cent of all user charge revenue in this assessment (agriculture represents about 40 per cent).

Some States and Territories also administer voluntary agricultural levies on behalf of the sector. These are in effect pass-through payments which should not affect State and Territory fiscal capacities.

Commission Staff Position

Staff propose to recommend the Commission:

ACT GOVERNMENT RESPONSE ON COMMONWEALTH GRANTS COMMISSION 2020 REVIEW DRAFT ASSESSMENT PAPERS

- Deduct all user charges from expenses because most relate to regulation activities and the same disabilities apply to expenses and revenue; and
- Collect data on State and Territory agricultural levies to confirm they are not material.

ACT Position

The ACT supports the staff proposals. The ACT's position on the treatment of user charges in general is set out in the chapter on Other Revenue.

Administrative Scale

Commission Staff Position

Commission staff proposed to retain the Administrative Scale assessment for this assessment but re-estimate the cost as part of the 2020 Review.

The Draft Assessment Paper notes that: "The ACT's costs are somewhat lower as its city-state nature means it has virtually no agriculture and mining industries and thus no need to provide some services."

ACT Position

The ACT supports the re-estimation of Administrative Scale costs as part of the 2020 Review. Our position on Administrative Scale is set out in detail in the chapter on that subject.

OTHER EXPENSES

Summary

Other Expenses captures all expenses which are not captured in the previous separate assessments, such as central agency expenses and natural disaster relief expenses.

The ACT considers many of the proposals that Commission staff have made regarding Other Expenses to be problematic for a variety of reasons. Such proposals include those to not assess national parks and wildlife services, which the ACT considers should continue to be assessed under the Services to Communities assessment, as well as the proposal to assess administrative scale expenses under the Other Expenses assessment, which the ACT considers should be captured under each relevant expense assessment for transparency reasons.

Further, the ACT considers that the Commission should reconsider its current approach of assessing natural disaster relief expenses on an APC basis, in order to account for substantial policy differences between States and Territories in relation to natural disaster mitigation and insurance.

The ACT does however support the Commission proposal to cease assessing grants to local governments for community amenities and regional development. We note that economic development expenses, which currently form part of the Services to Industry assessment and are assessed EPC and that the argument for retaining the assessment is contradictory with the Commission's position on other assessments.

Cross-border expenses are discussed in detail in the Cross-Border section of the Other Disabilities chapter.

Context

The Other Expenses assessment comprises expenses not separately assessed in other expense assessments. It includes:

- General public services — expenses for executive and legislative functions and administration of treasury, finance and other centrally provided services not connected to particular functions;
- Other services not assessed elsewhere — expenses for recreation, culture and religion (such as library and national park services), public safety services other than those provided by police (such as emergency services and fire protection) and support for local government services which cannot be allocated to a specific function;
- Miscellaneous purposes and transactions — public debt transactions and general purpose inter-government transactions that cannot be allocated to other purposes; and
- Natural disaster relief expenses.

The assessment also includes a location adjustment, recognising differences in regional costs faced by cities of similar remoteness, as well as expenses relating to:

- Administrative Scale allowances;

- Native title and land rights allowances; and
- National capital allowances except those relating to police.

Most of these expenses are classified to the service expenses component, which represents 90 per cent of the expenses in this assessment. With the exception of location disabilities, these expenses are assessed on an EPC basis. Differential assessments are applied to the remaining components as follows:

- Natural disaster relief – APC.
- Capital grants to local government – population growth.
- Administrative Scale – Commission estimates based on State and Territory data.
- Native title and land rights – APC.
- National Capital – Commission estimates.

The assessment for Administrative Scale is discussed in a separate chapter, while those relating to native title and land rights and national capital are discussed in the Other Disabilities chapter.

Natural Disaster Relief

Context

The current methodology assesses States' and Territories' net expenses for natural disaster relief under the NDRRA framework on an APC basis because the Commission considers that differences between the States and Territories under the framework are not subject to significant policy influences.

Commission Staff Position

Staff propose to recommend the Commission:

- Continue to assess natural disaster relief expenses on an APC basis;
 - Commission staff assert that assurance activities on State and Territory NDRRA expenditure claims conducted by EMA allow for greater confidence that States' and Territories' reported claims are comparable and eligible under the NDRRA framework;
- Not make an assessment for natural disaster mitigation expenses, due to the difficulty in obtaining expense data and identifying a reliable driver; and
- Continue to make adjustments to the adjusted budget to ensure:
 - Natural disaster relief expenses under the NDRRA framework are only assessed once;
 - Net natural disaster relief expenses funded from local government revenue are not included in the assessment because they do not affect State or Territory fiscal capacities; and

- Commonwealth NDRRA assistance payments through States and Territories to local government (for example, for roads) are not included in assessment expenses.

ACT Position

The ACT considers that the Commission should reconsider the approach currently taken to this assessment in light of substantial policy differences between States and Territories in relation to natural disaster mitigation and insurance. Although the NDRRA provides a common reporting framework and there is no evidence of inappropriate NDRRA claims by States and Territories, the APC approach to the assessment is too narrow and does not consider the impact of related State and Territory policies which impact on natural disaster relief costs.

Advice from the ACT Insurance Authority (ACTIA) is that implementation of additional mitigation measures should result in a lower insurance premium as the risk becomes more attractive to insurers. ACTIA has also advised that the traditional insurance market is now more open to providing other jurisdictions with cover for their roads networks than was the case in 2013, when QLD and SA attempted unsuccessfully to obtain such coverage. ACTIA has also stated that other options, such as parametric insurance (a form of insurance which does not indemnify the full loss to the insured party), are available.

Both mitigation and insurance measures raise a possible issue of a second order effect on expense needs for natural disaster relief, potentially warranting an adjustment to the GST distribution, if the impact is both quantifiable and material, to avoid any adverse incentive for reform. Such an approach would align with our proposed approach to tax elasticity adjustments.

The ACT supports the continuation of adjustments to the adjusted budget as outlined.

Capital Grants to Local Government

Context

The capital grants to local governments component was introduced in the 2015 Review to recognise the need for State and Territory support to local government for cultural and recreation facilities and community amenities. The assessment used population growth as the disability, as the Commission expected that States and Territories with above average population growth would incur higher costs. The assessment was not material by itself. However, it was included as the assessment of population growth in total was material. In the 2018 Update, the component did not redistribute more than \$3 per capita for any State or Territory.

Commission Staff Position

Recent analysis by Commission staff indicates that these grants are generally part of regional economic development programs and it is not apparent how States and Territories determine their level of support for these programs.

Staff propose to recommend the Commission cease assessing the capital grants to local governments for community amenities component because the driver of this spending is unclear.

ACT Position

The ACT supports the staff proposal for treatment of capital grants to local government for community amenities. We note that economic development expenses currently form part of the Services to Industry assessment and are assessed EPC.

We also consider that the argument for retaining the assessment on the grounds that population growth in total is material is not consistent with the approach taken by the Commission in other areas of assessment. For example, the Commission rejected the ACT's submission for continuation of the CSS adjustment as part of the Wage Costs assessment on grounds opposite to the argument adopted for this capital grants component.

National Parks and Wildlife Services

Context

The Commission does not currently make an assessment for national parks and wildlife services. Despite national guidelines on the establishment of designated protected areas, they consider that significant differences between States and Territories remain in the numbers of parks and areas protected. However, the Commission does acknowledge that the Commonwealth has had a major influence on the size of areas protected, particularly in TAS and the ACT.

They have also advised that the revised GFS system no longer has national park and wildlife services as a separate expense classification and it will instead be combined with other environmental protection expenses.

Commission Staff Position

Staff propose to recommend the Commission not assess national parks and wildlife services, due to uncertainties surrounding the policy influences and difficulty in obtaining reliable data to measure cost influences and expenses.

ACT Position

The ACT considers that national parks and wildlife expenses should be assessed as part of the Protection of the Environment assessment, even if they continue to be assessed EPC. This will improve the transparency of presentation of these expenses.

We are seeking further information from our line agency on whether drivers of national parks and wildlife expenses can be identified which are free of State and Territory policy influence and if so, what data sources would support measurement of their impacts on State and Territory expenditure on these functions. Any additional information we identify will be presented in a supplementary submission.

Cross-border Expenses

Cross-border expenses are discussed in the chapter on Other Disabilities.

Administrative Scale

Commission Staff Position

Commission staff are seeking advice from States and Territories on whether Administrative Scale expenses should be included as a component of the Other Expenses assessment or separately identified in each expense assessment.

ACT Position

The ACT is strongly of the view that Administrative Scale expenses should be separately identified in each expense assessment, to ensure that the full expenses for each assessment are accurately reported. This would align with the approach taken to other general disabilities such as location costs. It does not prevent the overall impact of the Administrative Scale assessments being separately reported as well.

Other Issues Including Location

Commission Staff Position

Commission staff have canvassed whether additional expenses, such as location costs, should be included in the Other Expense assessment if they continue to be assessed EPC, on the grounds that it simplifies the presentation of functional categories.

ACT Position

The ACT strongly opposes this suggestion, as we do for Administrative Scale. Although it may make the presentation of functional categories simpler, it also makes them less comprehensive and less transparent. It means the assessment presentation of such expenses can vary from year to year depending solely on whether the assessment is material or not, rather than on any substantive conceptual grounds.

User Charges

Commission Staff Position

Commission staff propose that user charges which are assessed EPC continue to be reported in the Other Revenue assessment on the grounds of simplicity.

ACT Position

The ACT strongly opposes the staff position on the current presentation of user charges as detracting significantly from the transparency of assessments. Our position on user charges is set out in detail in the chapter on Other Revenue.

PHYSICAL AND FINANCIAL ASSETS

Summary

The Physical and Financial Assets assessment equalises the capacity of the States and Territories to provide new physical and financial assets for their citizens and to depreciate existing assets.

The ACT is generally supportive of the Commission staff proposals on the overall structure of the Physical and Financial Assets assessment, including those to separately assess investment in all assessment and component service areas, remove the averaging of stock disabilities, using the assessment year's stock disability for both opening and closing asset stocks and using assessment specific growth measures for assessments in which reliable data are available.

The ACT also supports the Commission staff proposals on a number of other areas, such as continuing to assess the impact of population dilution on net financial assets, changing the Physical and Financial Assets assessment to a gross assessment and assessing the suitability of recurrent disabilities in assessing capital stock needs. We also do not oppose the Commission staff proposal to investigate whether land-related costs for larger cities are greater on a per capita basis than for smaller cities.

The ACT does not however support the Commission staff proposal to incorporate investment assessments into recurrent expense assessments, on transparency grounds. Further, we do not see the value of pursuing an attempt to quantify the relative costs and benefits of new versus old assets, on the basis that if the current valuations of assets are kept up to date, there should be no need to separately attempt to quantify their relative benefits generated or costs of maintenance.

Context

The current approach to assessment of capital spending was first implemented in the 2010 Review and is characterised as an "up-front" approach, which recognises needs when the expenditure actually occurs, rather than amortising them over the life of the asset.

There are three elements to the capital assessment:

- Net investment in **new physical assets** (gross fixed capital formation less depreciation);
- Depreciation (or **replacement of existing physical assets**); and
- Net borrowing (or lending) to change holdings of **net financial assets**.

These assessments provide States and Territories with equal capacity per capita to invest in new physical and financial assets and to depreciate existing assets in accordance with national average rates. Assuming that the equalisation process has been continuing over a long period of time, it maintains EPC stocks of physical and financial assets between States and Territories.

Under this approach, the main driver of differences in needs is population growth. Thus, States and Territories with relatively higher rates of population growth in the assessment years will gain GST compared with States and Territories which have relatively lower rates of population growth.

Net investment in physical assets (infrastructure) is assessed in four components (roads, urban transport, land and other services) because these components are considered to have different stock disabilities. Population growth as a driver applies across all of these components, except for land.

A further set of drivers, called “stock disabilities”, are based on the needs which are assessed for recurrent expenditure on the services supported by the infrastructure. SDC is the key driver of stock disabilities for social infrastructure, such as hospitals, schools and housing; while different stock disabilities apply to roads (heavy vehicle usage, road length) and to urban transport (population size and density of cities).

Finally, there is an assessment of input costs, or “cost disabilities”, which addresses differences between States and Territories in the cost of construction.

State and Territory holdings of physical assets are very large, comprising \$226 billion in roads, \$100 billion in urban transport and \$254 billion in other assets (e.g. hospitals, schools, social housing) (2016-17 figures), a total of around \$580 billion. This means that relatively small changes in disabilities (drivers) can cause large shifts in the GST distribution.

Net investment is, by its very nature, lumpy, with major fluctuations from year to year. This volatility is accentuated by sales and write-off of assets, which are also lumpy and operate to reduce net investment needs. On the other hand, depreciation is much more stable because it is driven by asset stocks, which do not change much from year to year.

Net borrowing/lending is driven by population growth. Population growth rates are subject to substantial fluctuations across States and Territories and over time, giving this element substantial volatility in its impact on the GST distribution.

Functionalising the Assessment

Context

The current assessment approach amalgamates needs across all of the ten assessments (Health, Schools Education etc.) within the other services component of net investment, which makes it difficult to identify the redistributive impacts by assessment. A functionalised assessment, where investment in every assessment is assessed separately, would make the assessment more transparent and easier to interpret. It would also enable the introduction of assessment specific growth factors, as described below (under *Refining the Assessment of Infrastructure Needs*).

Commission Staff Position

Staff propose to recommend the Commission separately assess investment in all assessment and component service areas. This could be presented as part of each individual assessment, part of the Physical and Financial Assets assessment or included in both.

ACT Position

The ACT supports the Commission staff proposal as it increases the transparency of the assessment. It will also enable the introduction of assessment specific measures of growth, which will increase the accuracy of the assessment.

We consider that needs for other service investment should be presented principally as part of the Physical and Financial Assets assessment, though they could also be presented in the relevant recurrent assessments for information.

Refining the Assessment of Infrastructure Needs

Context

The current assessment approach applies a three year averaging process for the end of year and beginning of year disabilities. This is a complex process which Commission staff claim reduces volatility only slightly. Moreover, it removes the alignment which occurs when changes in disabilities offset changes in population.

Total population growth is currently used as a global indicator of States' and Territories' need for investment across all assessments, with States and Territories with fast growing populations assumed to have greater investment needs than States and Territories with slow growing populations. A functionalised assessment would allow this measure to be refined to capture growth in the service use populations or asset requirements of each assessment specifically e.g. growth in government schools rather than overall population growth as the driver for investment in schools. However, reliable data on growth of service use populations may not be available for all assessments, in which case overall population growth would have to be used. This would need to take account of intercensal differences for each State and Territory identified following the 2021 Census.

The current assessment approach also aims to capture infrastructure needs relating to changes in State and Territory circumstances *within the year*. It does this by applying current year stock factors to end of year stocks and the previous year stock factors to start of year stocks. Commission staff have commented that some changes in cost allocations may not reflect "real world" changes e.g. they may reflect changes in data collection methods.

Commission Staff Position

Staff propose to recommend the Commission:

- Remove three year averaging of stock disabilities;
- Capture the change in circumstances through the use of assessment specific growth measures, where methods can be developed and reliable data are available. If no alternative measure is available, use total population growth as a proxy;
- Where population growth is used, specify change in population levels, rather than births, deaths and net migration, as the measure of population growth;
- Where there are considered to be additional stock requirements not captured by the growth indicator, use the assessment year's stock disability for both opening and closing stocks.

ACT Position

Three Year Averaging of Stock Disabilities

The ACT supports the Commission staff proposal to remove the averaging of stock disabilities. We can see no merit in the current approach. Stock disabilities are quite stable, as they depend on the underlying disabilities for recurrent expenditure assessments, such as SDC. The major cause of volatility in State and Territory shares is differences in population growth, which can be quite large.

For example, in the assessment years of the 2018 Update, the NT's population growth went from 0.0675 per cent in 2014-15 to 0.4814 per cent in 2015-16, an increase of over 600 per cent, while TAS's population growth went from 0.3430 per cent in 2015-16 to 0.5759 per cent in 2016-17, an increase of 68 per cent.

Assessment based on disabilities and population in the same assessment year is also in accordance with what is done in all other assessments and the three year averaging process of assessed needs across assessment years already addresses the year to year volatility issue.

Use of Assessment Specific Growth Measures

The ACT supports the Commission staff proposal to use assessment specific growth measures where reliable data are available, with total population growth to be used in assessments for which reliable data are not available. This will increase the accuracy of the assessment.

The ACT also supports the proposal to establish a method which uses change in population levels, rather than the components of growth (births, deaths, net migration), incorporating any intercensal difference into the measure, for total population growth. This would be in accordance with the decision taken by the Commission in the 2018 Update and supported by the ACT.

Use of Assessment Year's Stock Disability for Opening and Closing Stocks

The ACT supports the Commission staff proposal to use the assessment year's stock disability for both opening and closing stocks.

Again, we see no merit in attempting to capture *within year* change in stock factors (disabilities), an approach which is unlike that applied in any other assessment, for which States and Territories have only *one* assessed disability for a given assessment year. The current approach involves unnecessary complexity which does not improve the accuracy of the assessment.

Other Issues

Context

Privately Provided Assets

Commission staff have commented that smaller States and Territories may find it more difficult to attract private investment in "government type" assets compared with larger States. An example of this is toll roads in large cities, such as Sydney and Melbourne, for which substantial user charge revenue can be earned. Tolling is not feasible in smaller cities and towns with minimal road congestion problems. Staff are seeking State and Territory input on data which could enable such a disability to be assessed, if material.

New and Old Assets

Commission staff have also commented that the Investment assessment assumes that a new asset of a given value is equivalent to an existing asset of the same value. They state that the current assessment gives States and Territories the capacity to purchase a new asset (e.g. a new school) at the average depreciated stock value per capita i.e. to purchase a "new" depreciated asset.

They claim that this is not what States and Territories do or generally can do. Genuinely new assets are likely to have a higher value, as well as providing greater capacity and lower maintenance costs. Staff are seeking State and Territory input on how this issue should be handled.

Treatment of Land

Commission staff consider that Roads is the only assessment for which investment in land is large and the relevant disabilities are likely to be materially different from an EPC assessment. They have commented that, unlike the urban transport disabilities, the urban roads disabilities do not reflect higher costs for larger cities and will consider whether a better proxy of need can be developed.

Net vs Gross Investment

Commission staff have commented that depreciation is a proxy for expenditure on the replacement of existing assets. It is not a cash outlay but an accounting convention used to recognise the economic cost of the decline in value of assets over time. Staff note that the use and cost disabilities recognised in the Investment assessment are the same as those used in the Depreciation assessment and suggested that depreciation and net investment could be considered together in a single assessment of gross investment. This would simplify the assessment and reduce the possibility of negative net investment, which creates confusion from a presentation viewpoint.

Recurrent vs Capital Disabilities

Currently stock disabilities for all assessments excluding Roads and Transport are based on recurrent disabilities. Commission staff consider that these disabilities should be reviewed to determine whether they adequately reflect capital needs. This would include an examination of available data to support any changed approach.

Effect of Population Growth on Financial Assets

The Net Borrowing/Lending assessment has only one disability: population growth. Some States and Territories had suggested that population growth led to advantages as well as dilution (i.e. lower per capita stocks of financial assets due to population increase). A discount was incorporated in the assessment, partly because of uncertainty over this conceptual issue. However, subsequent Commission analysis of relevant data did not find evidence linking population growth and equity growth.

Commission Staff Position

Staff propose to recommend the Commission:

- Not consider differential assessment of investment in land for any assessment other than Roads;
- Assess the suitability of recurrent disabilities in assessing capital stock needs when assessments are further progressed;
- Consider whether to assess depreciation expenses with net investment expenses in an assessment of gross investment; and
- Continue to assess the impact of population dilution on net financial assets, remove the 12.5 per cent discount and not recognise any other disabilities.

ACT Position

Privately Provided Assets

The experience of the ACT is that we have found difficulty in attracting private capital to public projects in the ACT, particularly since the recent boom in the PPP and wider infrastructure market, which has attracted funds to larger projects in the big States. The ACT currently has a capacity constraint within its economy, estimated at around \$750 million per annum, for undertaking infrastructure projects, as well as limits on its ability to import skilled labour from NSW and VIC, which are undertaking major new infrastructure programs.

This is of concern given that the evidence provided by our line agency indicates a value for money advantage of about 10 per cent for the ACT's two PPP projects to date - the ACT Law Courts and Capital Metro Light Rail Stage One – compared with traditional delivery models.

There appears to be at least an anecdotal case for a disability for the relatively higher cost of attracting private capital to infrastructure projects in the smaller States and Territories. The ACT will consider whether such a disability can be quantified and may incorporate any findings in a supplementary submission.

New and Old Assets

The ACT does not see the value of pursuing an attempt to quantify the relative costs and benefits of new versus old assets. The valuation of an existing asset reflects its initial purchase or construction cost less depreciation (the reduction in its value over time). By definition, the flow of services from a depreciated asset is less than that of a new asset and the value of each is the net present value of the future flow of services (benefits) expected from the asset.

If the current valuations of assets are kept up to date, there should be no need to separately attempt to quantify their relative benefits generated or costs of maintenance, as the valuations already account for this. It does not seem to be an issue at the individual State/Territory level, provided all follow consistent, nationally standard methods of asset valuation. It should only be the national quantum which is at issue. That can only be based on the actual level of net investment and investment is by definition expenditure on *new* assets acquired during the course of an assessment year.

Treatment of Land

The ACT is not opposed to investigation of whether land-related costs for larger cities may be greater on a per capita basis than for smaller cities. However we note comments made by NSW at the telepresence held on 4 October 2017 that the main additional cost impact of new infrastructure in major cities is a requirement for more complex infrastructure, such as tunnels, rather than more land or higher land-related costs.

Net vs Gross Investment

The ACT supports assessing investment on a gross basis by incorporating depreciation into the capital assessment and removing it from recurrent assessments. The treatment of depreciation as a recurrent expense is an accounting convention, which does not represent real outlays and, in that regard, unlike any other expenditure assessed by the Commission. It is a means of representing the decline in value of existing capital and its inclusion in the capital assessment as an expense is appropriate.

Our view is consistent with the position we took during the 2015 Review that a gross assessment of investment would be simpler, more consistent with the up-front approach for new investment and would overcome perceptions of double counting.

Recurrent vs Capital Disabilities

The ACT supports the Commission staff proposal to assess the suitability of recurrent disabilities in assessing capital stock needs when assessments are further progressed.

Effect of Population Growth on Financial Assets

The ACT supports the Commission staff proposal to continue to assess the impact of population dilution on net financial assets, remove the 12.5 per cent discount and not recognise any other disabilities.

Cost Factors

Context

In the 2015 Review, the Commission introduced a construction cost index to measure capital costs. This was based on the construction cost indices published by Rawlinsons. The Commission recognised that these indices may not represent the full costs associated with constructing some assets such as hospitals and roads and did not cover investment in equipment. As a result, they used an average of the construction cost indices and recurrent wage and regional cost factors.

Commission Staff Position

Staff propose to recommend the Commission retain the 2015 Review method of assessing capital costs through a combination of construction cost indices and recurrent cost factors.

ACT Position

The ACT supports the Commission staff proposal.

Presentation

Context

Commission staff have indicated that functionalising the assessment of investment expenses, with the separate calculation of investment needs for each assessment, raises the question of whether investment in each recurrent assessment (e.g. Schools Education) is best treated as part of the relevant recurrent expense assessment, rather than the Physical and Financial Assets assessment. However, they have cautioned that assessing investment within recurrent expense assessments will likely introduce volatility to the recurrent assessments and dominate redistribution in an assessment.

Commission Staff Position

Staff propose to recommend the Commission determine the best presentation framework based on staff and State and Territory recommendations.

ACT Position

The ACT does not support incorporating investment assessments with recurrent expense assessments. The introduction of functionalised investment assessment is what provides the increased transparency discussed above, whereas merging capital and recurrent expenses does not add to transparency and may actually detract from it.

**ACT GOVERNMENT RESPONSE ON COMMONWEALTH GRANTS COMMISSION 2020
REVIEW DRAFT ASSESSMENT PAPERS**

A functionalised presentation in the Physical and Financial Assets assessment will make it easy to identify the investment relating to each recurrent expense assessment.

DISABILITY ASSESSMENTS

WAGE COSTS

Summary

The Wage Costs disability captures the additional costs faced by States and Territories from paying higher wages and salaries to their employees as a result of the broader economic conditions of their jurisdictions. As well as the economic conditions of individual States and Territories, the ACT has consistently maintained that State and Territory public sector wages are also influenced by national public sector labour markets.

The ACT is supportive of the Commission staff proposal to retain its methodology for assessing Wage Costs, updated for the latest CoES and GFS data. However, we do not support the Commission staff proposal to discount the Wage Costs disability, as we consider that improved data is now available to support the assessment and that concerns about how accurately the model controls for productivity differences and how well private sector wages proxy public sector wage pressures are not well-founded.

The ACT considers that there is a substantial case for an adjustment which recognises the influence of the APS on ACTPS wages. We are carrying out further investigation and reserve the right to present supplementary information to the Commission on this issue at a later date.

The ACT also reiterates its case for a reinstatement of the Wage Cost disability for the additional costs faced due to the legacy of the CSS and PSS first raised as part of our response to the Commission's New Issues Paper for the 2018 Update. We again emphasise that there is evidence to suggest a significant cost differential between the CSS and PSS and State and Territory defined benefit superannuation schemes and that the ACT had no effective policy choice in its continued allowance of access to the PSS and CSS. The ACT recommends that the Commission continue to assess a Wage Cost disability for the PSS and CSS in the 2020 Review.

Context

Wages and salaries represent the largest component of State and Territory expenditure and account for a significant share of expenditure in nearly every expense assessment. The Wage Costs assessment addresses a global disability, rather than the expenses associated with an individual assessment of service delivery (such as schools or health spending).

The Commission models the wages of the average private sector worker in each State and Territory, controlling for differences in the characteristics of that worker that are known to affect wage levels, such as work experience and qualifications. The model also adjusts for States' and Territories' composition of industry and occupations.

An additional variable for State or Territory of residence is used to estimate the influence that State or Territory of residence has on the wages of comparable individuals. The wages paid to comparable private sector workers are used as a proxy for the pressures on public sector wages in each State and Territory.

Commission Staff Position

Commission staff consider that there are no major issues in the Wage Costs assessment for the 2020 Review.

The assessment is supported by a sound conceptual case and evidence that public and private sectors are responsive to the same underlying influences in labour markets. The econometric model uses reliable data and has been found to be fit for purpose by several consultants previously engaged by the Commission.

Staff propose to recommend that the Commission:

- Retain its approach to estimating differences in Wage Costs using the 2016 Update econometric model, updated with new CoES data each year; and
- Update the wage proportions of service delivery expenses based on GFS expense data in the 2020 Review, but not update these proportions in subsequent Updates.

ACT Position

The ACT supports the Commission staff proposals as far as they extend, but proposes some enhancements to the assessment which relate to cost drivers specific to the ACT.

Other Issues Considered

Context

National Markets

Some States and Territories have argued that they have to respond to national labour market pressures and that they explicitly compare their wage levels with those in other States and Territories. To the extent that this was average policy and results in more uniform interstate wage levels, it could mean that the fiscal capacities of States and Territories do not diverge for wage related reasons.

Influence of the Commonwealth Public Sector

The very large size of the Commonwealth public sector in the ACT makes the ACT quite unlike any other jurisdiction in the composition of its employment base. This means that the use of private sector wages alone as a proxy for public sector wages does not accurately represent public sector wage pressures in the ACT. The significance of the Commonwealth Government in the ACT and its impact on the ACT labour market is clearly illustrated in Part C of this submission (in particular see Figures C.1 and C.2; pp.52-53).

Cost of the Public Sector Superannuation Scheme

In its response to the 2018 Update New Issues paper issued by the Commission, the ACT argued for an adjustment to the Wage Costs assessment to recognise the higher costs imposed on the ACT by the Public Sector Superannuation Scheme (PSS), which was inherited from the Commonwealth at the time of the establishment of a separate ACTPS in 1994.

Commission Staff Position

National Markets

The Commission did not consider that the available data were consistent with uniform interstate wage levels, nor did it accept the view held by some States and Territories that there exists a significant suite of public sector roles where wages are set at a purely national level.

The consultant engaged by the Commission in the 2016 Update process found some evidence that States and Territories compete in both a national and a local labour market simultaneously, implying that States and Territories set wage levels with reference to the wages of private sector workers in their own State or Territory as well as to the wages paid to comparable public sector workers in other States and Territories.

The Draft Assessment Paper quotes Census data showing that 60 per cent of people joining the State and Territory public services between 2006 and 2011 moved from the private sector in their State or Territory, while only three per cent moved from the public service in another State or Territory.

The Commission concluded (in the 2016 Update) that the direct impact of competition for labour from other sectors within a State or Territory appeared to be stronger than the impact of a national labour market for State and Territory public service employees.

Commission staff have asked for State and Territory views on data or methods that might allow the Commission to measure the influence of national markets on the level of wages paid.

Discounting the Assessment

The modelled outcomes of the regression used in the assessment are discounted by 12.5 per cent because the Commission considers there is some uncertainty about how accurately the data capture Wage Costs, how accurately the model controls for productivity differences and how well private sector wages proxy public sector wage pressures.

ACT Position

National Markets

The ACT has consistently maintained that State and Territory public sector wages are influenced both by national public sector labour markets and by local/regional private sector labour markets. Moreover, the existence of national labour markets in no way precludes actual wages including premiums or discounts to a national average which represent differences between States and Territories in locational costs and amenities. On the assumption of a fairly high level of labour mobility between States and Territories, nominal wages adjusted by these locational costs and amenities should equate real wages across States and Territories ("real" being broadly defined to include non-wage benefits and costs). On the other hand, if labour mobility between States and Territories is low, then the existence of national labour markets can be considered minimal or irrelevant.

Discounting the Assessment

The ACT does not support the continuation of the 12.5 per cent discount applied in this assessment, both because of the improved data which are now available to support the assessment and because we consider that concerns about how accurately the model controls for productivity differences and how well private sector wages proxy public sector wage pressures are not well-founded.

The Commission originally applied the 12.5 per cent discount to this assessment on the grounds of data uncertainty. We note that, in its New Issues Paper for the 2017 Update, the Commission commented that “the next few updates were likely to incorporate higher quality contemporaneous data”.

The concern over controlling for productivity differences is exaggerated, if not completely unfounded. The model as currently applied controls for composition of industry and occupation, which are major factors driving productivity differences between workers.

It also controls for variables at the individual level which impact on productivity such as work experience and qualifications. In combination, these adjustments should ensure that productivity related differences between States and Territories have minimal impact on the residual variations.

The latest available data for relative public and private sector wages across States and Territories (Table D.9) show a strong correlation of 0.83 between public and private sector wages, reinforcing the view that private sector wages are a good proxy for public sector wage pressures – see table below for wage differentials from the national average.

Table D.9: Relative Wages vs National Average by State or Territory and Sector 2016-17

State/Territory	Private Sector	Public Sector	Correlation
NSW	0.00	0.01	
VIC	-0.01	-0.03	
QLD	-0.01	-0.01	
WA	0.05	0.06	
SA	-0.02	-0.04	
TAS	-0.08	-0.05	
ACT	0.07	0.01	
NT	0.07	0.08	
			0.83109543

Given these considerations, the ACT’s position is that there is no longer a case for maintaining any discounting of this assessment, either on grounds of data uncertainty or methodological issues.

Influence of the Commonwealth Public Sector

The ACT requests that the Commission review the influence of the APS on ACT Government wages. An adjustment for this reason was previously recognised by the Commission, but was terminated from the 2011 Update primarily because the SET data could not differentiate between Commonwealth Government employees and State and Territory Government employees.

While the ACT recognises the Commission's preference, where possible, to avoid making State/Territory-specific adjustments to assessments, this policy should not be pursued rigidly at the expense of accuracy of equalisation, provided there is a sound conceptual case for an adjustment and reliable data are available. We consider that these criteria apply to the proposed adjustment for a Commonwealth public sector influence on ACT Government Wage Costs.

We are carrying out further investigation and reserve the right to present supplementary information to the Commission on this issue at a later date.

Cost of the Public Sector Superannuation Scheme

During the 2018 Update process the ACT put forward an argument for the reinstatement of the disability for the additional costs of the CSS, as well as an expansion of the disability to capture the additional costs imposed by the PSS. This argument was advanced in the context of the Commission Staff Discussion Paper CGC 2017-20-S *New Issues for the 2018 Update*.

The ACT argued that since the issue of the PSS was last examined during the 2004 Review, the cost of servicing superannuation liabilities for members of the PSS had significantly increased compared with those for similar defined benefit superannuation schemes operated by the States and the NT. We noted that the NECR of the PSS for the ACT Government had increased from 15.4 per cent in 2002-03 to 19.8 per cent in 2016-17. This increase in the NECR of the PSS had resulted in the PSS NECR being 3.9 percentage points higher than the CSS NECR and 8.5 percentage points higher than a weighted average of the defined benefit superannuation schemes of NSW and VIC.

Moreover, the ACT argued that we had no control over whether we could remove access to the PSS on the basis of agreements made between the ACT Government, Commonwealth Government and labour unions at the time of self-government. These agreements stipulated that the ACT maintain access to the PSS for APS employees moving into the ACT Government. These agreements also mandated that legislation governing Commonwealth employment conditions be treated as ACT legislation. These factors effectively prevented the ACT from closing access to the PSS until 1 July 1994, the date of the establishment of the ACTPS.

The ACT also noted the failure of its attempts to close access to the PSS from 1997 to 1999 due to industrial action taken by labour unions in the AIRC. After a review of the ACT's superannuation arrangements in September 1997, the ACT Government announced in May 1998 that superannuation choice arrangements would be implemented and the PSS closed to new employees from 1 July 1999. The ANF, on behalf of a number of unions, initiated AIRC hearings to prevent the PSS closure. The outcome of these hearings was that the ACT Government abandoned its attempts to close access to the PSS, on the grounds that if it had not done so, the AIRC would have issued, at minimum, a direction to the ACT Government forcing it to retain access.

Given the very substantial increase in the NECR of the PSS in recent years and the history of the PSS since self-government in the ACT, we considered (and still consider) that the PSS imposes a significant and unavoidable additional cost on the ACT. However, the Commission, in the 2018 Update, rejected the ACT's arguments on the grounds that the ACT had control over its superannuation arrangements from the establishment of the ACTPS and that the cost of similar defined benefit superannuation schemes in the States and the NT were also high, thus suggesting that an adjustment would be immaterial.

The Commission did not elaborate further on its decision, nor did it provide any quantitative analysis indicating that the cost of the PSS was not materially higher than similar defined benefit superannuation schemes.

The ACT asks the Commission to comprehensively review its position on our arguments within the context of the 2020 Review. We request that the Commission present quantitative analysis on the impact of assessing the additional costs imposed by the PSS on the GST distribution, indicating clearly whether the impact is or is not material on the basis of State and Territory data on the NECRs and membership of defined benefit superannuation schemes. We also ask the Commission to elaborate further on its position that the ACT had policy control over access to the PSS after the establishment of the ACTPS, including its response to the information presented by the ACT on the AIRC hearings on this issue.

GEOGRAPHY USED BY THE COMMISSION

Summary

The Commission utilises a variety of different measures and approaches to measure how different geographical attributes impact on the cost to the States and Territories of service delivery, including remoteness, indigeneity and community size. These impacts are captured in the indigeneity, SDS and remoteness disabilities.

The ACT understands the conceptual validity of the SDS disability. However, we consider that the method used to measure the disability separately from regional costs is not robust, noting also that SDS is strongly correlated with regional costs and only has a material impact on the GST distribution of the NT. The Commission should consider whether these two disabilities should be merged to form a single disability.

We are also concerned about the overlap between the remoteness and regional costs factors, given that remoteness includes both use and cost disabilities and consider that the methods currently used by the Commission to address this issue lack robustness.

The ACT supports the Commission staff position that person-based measures of SES are likely to be better predictors of disadvantage and service use than area-based measures. We note, as was discussed in the Special Circumstances of the ACT chapter, that the ACT has a much greater than average diversity in SES at the SA1 level, which masks the level of individual disadvantage. We consider that it would be preferable to replace area-based measures of SES with individual or household-based measures, though note that data availability may make this difficult. To the extent that area-based rather than individual or household based measures have to be used, we support the use of SEIFA and NISEIFA for the total and non-indigenous populations, respectively.

The ACT is broadly supportive of other proposals relating to geography by Commission staff, including those to continue using ABS remoteness areas geography across all assessments, continuing to apply a regional cost disability to services based on school, police, post-secondary education and hospital data where applicable, continuing to assess cross-border non-wage costs and to look into the merits of IRSEO+ as a better measure of indigenous SES.

Context

The Commission uses different geographic classifications and approaches to measure different attributes affecting service delivery costs.

- ABS remoteness areas to measure:
 - Regional costs, which capture the cost of delivering comparable services in more or less remote areas; and
 - The different use of services by people in more or less remote areas as part of SDC in various expense assessments.
- SDS, which measures the additional cost of delivering services in small isolated communities where the economies of scale of larger centres are not possible.
- Three area-based measures of SES are used.

- SEIFA IRSD is an ABS published dataset used where indigenous splits are not required.
- IRSEO, developed by CAEPR at the Australian National University.
- NISEIFA, produced for the Commission by the ABS, applying ABS methods for SEIFA to the non-indigenous population.

Commission Staff Position

The Commission states that the cost of delivering the same level of service may vary because of regional differences affecting the cost of inputs (as distinct from differences in levels of use i.e. demand). Conventionally, the Commission distinguishes between use disabilities, such as SDC, which may be thought of as demand-side factors and cost disabilities, such as regional costs, which may be thought of as supply-side factors.

SDS is also recognised as a separate disability, defined as diseconomies in the provision of certain services to small isolated communities because of the indivisibility of labour and unproductive travel time. Towns relatively close to major cities (i.e. not remote) can still be sufficiently isolated to suffer diseconomies of scale, while some large towns are remote from major cities, but large enough not to also incur diseconomies of scale.

ACT Position

Service Delivery Scale

The ACT understands the conceptual validity of the SDS disability. However, we consider that the method used to measure the disability separately from regional costs is not robust. The Commission should consider whether these two disabilities should be merged to form a single disability. SDS redistributes only \$83m in GST, compared with a redistribution generated by regional costs of \$1,034m in GST (2018 Update). It has a material impact only in the NT (\$84 pc), with no other State or Territory gaining or losing more than \$14 pc. These two factors have a correlation of 0.91 as at 2018-19 (Table D.10).

We note that the Commission stated in relation to the Schools assessment in the 2015 Review that: “the combined SDS and regional costs results suggest some portion of costs considered to reflect SDS effects in the 2010 Review are now allocated to the regional cost effects in the 2015 Review”¹⁵. The only State or Territory (NT) experiencing a material impact from the SDS assessment gains a similar percentage in redistribution from both factors.

¹⁵ Commonwealth Grants Commission 2015 Review Report Vol 2, p.483.

Table D.10: Correlation of redistribution for regional costs and SDS

Disability	NSW	VIC	QLD	WA	SA	TAS	ACT	NT	TOTAL
Regional Costs (\$)	-508	-461	306	215	90	129	-64	295	1,035
Per cent of redistribution	-49.08	-44.54	29.57	20.77	8.70	12.46	-6.18	28.50	100
Service Delivery Scale (\$)	-29	-49	12	22	25	4	-5	21	84
Per cent of redistribution	-34.52	-58.33	14.29	26.19	29.76	4.76	-5.95	25.00	100
Correlation (\$)									0.914858

Source: 2020 Review, Staff Draft Assessment Paper CGC 2018-01/23-S, Table 1, p. 5.

Area vs Individual Based Measures

The ACT notes the Commission staff statement that: “...person-based measures of SES such as income or educational attainment are likely to be better predictors of disadvantage and service use [than area-based measures]”. We agree with this statement. It is further reinforced in the Assessment Paper’s discussion of the size of the indigenous areas used as the basis for IRSEO, which notes that Brisbane city is a single indigenous area, classified in the “least disadvantaged” category, but “while there are pockets of disadvantage in some areas/suburbs, the aggregated geographic classification used masks such disparities” (para 66, pp. 15-16.). This is the same situation as applies in the use of SEIFA areas in the ACT; the ACT has a much greater than average diversity in SES at the SA1 level, which masks the level of individual disadvantage.

We recognise that the ACT is distinguished by having a much higher proportion of high SEIFA areas than the national average and a very much lower proportion of low SEIFA areas (Table D.11). However, the proportion of ACT residents belonging to SEIFA Group 1 is consistently higher than the national average across all SEIFA deciles from decile 2 onwards, being particularly significant (at a 5 per cent level) for SEIFA deciles 6, 7 and 8. These data indicate the “masking” effect mentioned above. We contend that this characteristic is likely to be most significant in measuring need for services targeted at low SES individuals and households (e.g. via means testing), for which area-based measures will tend to underestimate the level of disadvantage in the ACT.

**ACT GOVERNMENT RESPONSE ON COMMONWEALTH GRANTS COMMISSION 2020
REVIEW DRAFT ASSESSMENT PAPERS**

Table D.11 – Percentage of SEIFA decile areas by SEIFI group – ACT and National

SEIFA IRSD Decile	1	2	3	4	5	6	7	8	9	10
SEIFA Group	ACT Percentage									
1	42.28	33.88	27.13	23.98	20.87	19.03	15.46	12.75	9.34	5.22
2	7.81	8.55	10.66	12.17%	12.32	13.85	12.88	12.37	11.96	8.79
3	21.59	21.45	26.52	28.26	30.07	31.16	32.28	33.53	34.49	34.07
4	28.32	36.12	35.69	35.58	36.74	35.97	39.38	41.35	44.21	51.93
	National Percentage									
1	45.40	31.50	26.50	22.70	19.80	16.90	14.40	11.90	8.90	5.20
2	19.10	22.50	23.00	22.30	22.20	21.60	20.30	18.60	16.50	12.60
3	19.70	25.90	28.50	30.10	31.40	32.70	33.60	34.30	34.90	34.60
4	15.90	20.00	22.00	24.80	26.70	28.90	31.70	35.30	39.70	47.60
ACT vs National	0.7505	0.2107	0.0541	0.4879	0.6671	0.8034	0.8928	0.9533	0.9840	0.9943

Source: ABS (special request)

It would be preferable, were the required data available, to replace area-based measures of SES with individual or household-based measures, removing the need for indexes such as SEIFA, IRSEO and NISEIFA. However, in practice this option is limited by lack of data on the income or educational attainment of individual service users.

Therefore, even if the SEIFI index were to be updated by the ABS with 2016 Census data (as suggested in the Welfare assessment paper, para 38, p.12), an individual-based assessment could not be implemented without the required data allowing the SES of service users at the individual (or household) level to be determined.

We intend to request further feedback from our line agencies on the availability of such data for specific services, and ask that the Commission consider making a similar request of other States.

Remoteness and Regional Costs

A further concern is the overlap between the remoteness and regional costs factors, given that remoteness includes both use and cost disabilities. Although Commission staff acknowledge this concern and have attempted to address the issue in the expense assessments, it is far from clear how robust those methods are. The table below, extracted from the 2015 Review report, shows that remoteness and regional costs are both assessed for a number of major expense assessments, including Health, Schools Education, Welfare, Housing and Services to Communities.

The Draft Assessment Paper reinforces this concern in its discussion of cost gradients (para 55, p.14), commenting that it would seek to adopt a measure “with the least prospect of double counting higher service use in remote areas and the greatest chance of being a pure cost gradient”. Regressions which are designed to predict hospital and schools funding by remoteness category (see discussion on p.9 of the Draft Assessment Paper) also risk confounding use and cost factors, with double counting potentially arising as a result.

ACT GOVERNMENT RESPONSE ON COMMONWEALTH GRANTS COMMISSION 2020 REVIEW DRAFT ASSESSMENT PAPERS

The ACT considers that the Commission should review the remoteness and regional costs measures, in consultation with States, to ensure that they are as robust and credible as possible.

Table D.12 - Summary of disabilities measured in each expense category (a)

Category	Indicator of State shares	Disaggregated use attributes						Other disabilities assessed (b)					
		Indigenous status	SES	Remoteness	Age	Urban/Rural pop	Population growth	Non-State sector	Wage costs	Regional costs	Service delivery scale	National capital	Cross-border
Schools education	Student numbers	X	X	X		X		X	X	X	X		
Post-secondary education	Population	X	X	X	X				X	X			X
Health	Population	X	X	X	X			X	X	X			X
Welfare	Population	X	X	X	X				X	X	X		X
Housing	Households	X	X	X					X	X			
Services to communities	Population	X		X					X	X	X		
Justice	Population	X	X		X				X	X	X	X	
Services to industry	Sector size, number of establishments and private sector investment								X	X			
Roads	Length and use of roads					X			X	X			
Transport (c)	Population					X			X	X			
Other expenses	Population						X		X	X		X	X
Depreciation (d)	Assessed stock												
Investment (d)	Assessed stock						X						
Net borrowing	Population						X						

Source: Commonwealth Grants Commission 2015 Review Report, Vol. 2, p. 32.

- (a) Administrative Scale costs and native title and land rights disabilities for all assessments and natural disaster and capital grants for local government expenses are assessed in the Other Expenses category.
- (b) Some disabilities only apply to a proportion of the category. For more information, please refer to each category assessment chapter.
- (c) The population living in cities of different sizes is an influence recognised in this category.
- (d) The Infrastructure assessments use relevant category specific use disabilities to calculate assessed stock. A capital cost disability is also applied. The disabilities used are described in the Infrastructure assessments chapter.

Geography for Regional Costs Assessment

Context

Currently the Commission uses ABS standard remoteness areas based on ARIA.

They have examined an alternative measure of remoteness; the MMM, which was originally developed for the Commonwealth Department of Health to target incentive payments for rural doctors.

Commission Staff Position

Staff propose to recommend the Commission continue using ABS remoteness areas geography across all assessments.

Commission staff found that, although the MMM has a finer breakdown of inner and outer regional areas than ARIA, there was little difference in average funding per student (in the Schools Education assessment) across the additional categories in the MMM. A similar pattern was found in applying MMM to data on hospital admissions.

ACT Position

The ACT supports the Commission staff position given the lack of additional discriminatory power offered by alternative measures to ARIA.

Broadening Evidence Base on Regional Costs

Context

In the 2015 Review, the Commission measured regional costs in schools and police and extrapolated from the experience of these services to other services. Other services are delivered in a very different way. Staff consider that broadening the evidence base for the regional costs assessment is important for the 2020 Review.

Commission Staff Position

Staff propose to recommend the Commission:

- Develop a regional costs assessment using data from schools, police, post-secondary education and hospitals; and
- Test whether there are significant differences in the cost gradients between these services and, if not, use a single measure for all assessments.

Staff propose to recommend the Commission:

- Send a data request to States and Territories for current data on State and Territory spending by region by service; and
- Continue applying a regional cost disability to services where a conceptual case has been identified.

ACT Position

The ACT supports the Commission staff position, with the reservation that, as discussed above, there should be clarity in distinguishing cost factors from use factors in the development of cost gradients.

The proposed data collection relating to regional costs is not likely to involve the ACT.

Measure of Indigenous Socio-economic Disadvantage

Context

In the 2015 Review the Commission adopted IRSEO as the geographic socio-economic index for the indigenous population, in order to address the ToR requirement to capture the changing characteristics of the indigenous population. However, some States and Territories have raised concerns about technical aspects of IRSEO.

A key concern was that IRSEO was constructed to measure the positive aspects of SES, rather than socio-economic disadvantage. Commission staff consider that, for most variables used in IRSEO, advantage and disadvantage are the inverse of each other. A related concern was that SEIFA uses some additional indicators of advantage/disadvantage and that therefore it did not align with IRSEO. Advice from experts in the field is that indigenous disadvantage is different from non-indigenous disadvantage, so the differences between the indexes are appropriate.

IRSEO is calculated based on indigenous areas rather than the SA1s that form the basis of SEIFA. The larger geography used for IRSEO reflects the smallest consistent geography with sufficient indigenous population to produce reliable estimates across all areas. This can result in a masking of the level of disadvantage in areas with a very large indigenous population e.g. Brisbane city.

CAEPR at the Australian National University, which developed IRSEO, is currently working on a revised version, known as IRSEO+. This involves a new, purpose-built geographic classification which will be more disaggregated than indigenous areas. CAEPR are also considering developing an index based on a regression predicting aspects of State and Territory service use, as well as a variable on *change* of indigenous identification between the 2011 and 2016 Censuses – this is seen as a possible discriminator in relation to indigenous SES.

Commission Staff Position

Staff propose to recommend the Commission look into the merits of IRSEO+ as a better measure of indigenous SES once this becomes available.

ACT Position

The ACT supports the staff proposal.

Other Issues Considered

Context

SDS captures the impact of diseconomies of scale stemming from service provision being on a smaller scale in isolated areas than in more accessible areas. The Commission defines SDS areas as those more than 50 km from towns of 5,000 people based on analysis of Census data staffing patterns for school and police services. These SDS estimates are extrapolated to the assessments for Services to Communities, courts and family and child welfare services. Commission staff acknowledge the conceptual simplifications in the assessment, but consider that changes would be unlikely to materially improve the assessment.

Commission staff consider SEIFA and NISEIFA are the most appropriate area-based measures of SES for the total and non-indigenous populations, respectively.

In the 2015 Review the Commission made a judgement-based assessment of interstate non-Wage Costs which provided for higher costs faced by small cities which have some characteristics of regional areas as well as of capital cities. The ACT received a positive adjustment of \$30 million from this assessment.

Commission Staff Position

Staff propose to recommend the Commission:

- Continue to use SEIFA and NISEIFA for the total and non-indigenous population, respectively; and
- Maintain 2015 methods for SDS; and
- Maintain 2015 methods to measure interstate non-wage costs.

ACT Position

The ACT has reservations about the use of area-based indexes to assess socio-economic disadvantage, as set out above. However, to the extent that area-based rather than individual or household based measures have to be used, we support the use of SEIFA and NISEIFA for the total and non-indigenous populations, respectively. As also stated above, the ACT considers that SDS is a flawed concept and that consideration should be given to merging it with the regional costs disability.

The ACT supports the staff proposal for assessment of interstate non-wage costs.

ADMINISTRATIVE SCALE

Summary

The Administrative Scale disability recognises the costs States and Territories incur in delivering services which are independent of the size of the service population. Administrative Scale costs are the minimum fixed costs which do not vary with service populations. Conceptually, the case for such costs lies in the fact that States and Territories with lower populations have a higher per capita cost since the minimum functions of government are spread over a smaller number of residents. The administrative scale assessment provides an allowance for such a scenario.

- The ACT supports the Commission staff recommendation to retain the definition of administrative scale, as outlined above.
- We support the Commission staff recommendation to re-estimate administrative scale expenses for each expenses category using the bottom-up and top-down approaches.
- We support the Commission staff recommendations to adjust the Administrative Scale expenses for the ACT to account for the services which have zero or low needs in the ACT, and to decide on whether a separate recognition of indigenous service delivery is warranted for the NT based on other States' and Territories' responses.
- We support the Commission staff recommendation to re-estimate the Wage Costs factor for administrative scale costs based on States and Territories' data for their head offices and whole-of-State/Territory functions.
- The ACT supports the Commission staff recommendation to index the administrative scale expenses in the context of relativity updates by using the ABS SLGFCE deflator.
- We support the option to separately identify Administrative Scale expenses in each expense assessment. A view of the total impact of the Administrative Scale disability on GST distribution, as provided currently, should also be retained for presentation purposes.

Context

The Administrative Scale disability recognises the costs States and Territories incur in delivering services which are independent of the size of the service population. The costs are measured on the basis that States and Territories follow average policies and operate with average efficiency in delivering those services. Costs within the ambit of Administrative Scale costs include:

- Costs of core head office functions of departments (e.g. corporate services, policy and planning functions, exclusive of staffing and other resource costs incurred in delivering services); and
- Costs of services that are provided to the whole of State/Territory (e.g. the legislature, the judiciary, the Treasury, the revenue office etc.), but not all staffing and other resource costs associated with delivering them.

It is worth noting that Administrative Scale is not an assessment of all fixed costs or 'non-front line services'. Neither does it have anything to do with economies or diseconomies of scale. It is an assessment of minimum fixed costs which do not vary with service populations. The other fixed costs are taken into account in the service delivery component of expense assessments and assessed according to the relevant disabilities.

As the Administrative Scale assessment reflects the costs of providing services independent of the population being serviced, the quantum of such costs is the same across all States and Territories, barring some minor adjustments for the ACT and the NT. Hence, conceptually, the case for Administrative Scale costs lies in the fact that States and Territories with lower populations have a higher per capita cost since the minimum functions of government are spread over a smaller number of residents.

Table 1 of the Draft Assessment Paper shows the Administrative Scale impacted expenses for 2016-17 by assessment, with \$2.1 billion being the total of assessed Administrative Scale expenses across all States and Territories. These Administrative Scale expenses are based on estimates done as a part of the 2004 Review and have been indexed using the ABS SLGFCE deflator since then.

In the 2015 Review:

- Adjustments were made to the ACT's and the NT's Administrative Scale costs on the following grounds.
 - The ACT has zero or very low needs with regard to non-urban transport, primary industry and mining, services to indigenous communities and fuel and energy. Hence, the ACT's assessed Administrative Scale expenses for categories in which such services are provided were reduced by \$10.9 million in 2016-17.
 - The NT is considered to provide an above average level of service in the areas of education, health, welfare, housing and services to communities since it operates a dual service delivery model for its indigenous and non-indigenous residents. Hence, the NT's assessed expenses were increased by \$7 million in 2016-17, for the categories in which such services are provided.
- The Wage Costs factor was applied to 80 per cent of the Administrative Scale expenses.

In the 2018 Update, the Administrative Scale disability redistributed \$920 million of GST from an EPC share. The ACT gained \$243 million above its population share of GST due to the Administrative Scale assessment.

Commission staff discuss the issues and analysis applicable for this assessment for the 2020 Review under the following heads:

- Conceptual case for Administrative Scale and its definition;
- Re-estimation of Administrative Scale costs;
- Adjustments for the NT and the ACT;
- Wage Costs adjustment;
- Indexation of Administrative Scale expenses; and

- Presentation.

Conceptual Case and Definition of Administrative Scale

Context

Commission staff and most States and Territories consider the conceptual case for Administrative Scale and its definition are settled. NSW and WA have expressed some contrary views regarding the existence of economies or diseconomies of scale in the provision of head office and whole-of-State/Territory services. However, Commission staff do not intend to pursue such issues as they are clear that conceptually, Administrative Scale costs are not related to economies or diseconomies of scale.

Commission Staff Position

Staff propose to recommend the Commission to retain the 2015 Review definition of Administrative Scale.

ACT Position

The ACT supports the Commission staff recommendation. We agree that the definition of Administrative Scale is clear and so is the concept and we do not see any merit in revisiting any aspect.

Re-estimating Administrative Scale Costs

Context

In Staff Research Paper CGC 2017-06-S *Administrative scale*, Commission staff proposed to re-estimate Administrative Scale costs through two main approaches namely, the bottom-up approach and the top-down approach.

- The bottom-up approach involves derivation of a basic structure and staffing for any given department/function followed by costing; and
- The top-down approach makes estimates by reference to the size of head offices and whole-of-State/Territory services in the smallest States and Territories, after removing any staffing/expenses considered inconsistent with the average minimum structure.

These approaches are similar to those followed in the 1999 and 2004 Reviews. Other approaches attempted in past Reviews, such as regression analysis, were unsuccessful. The research paper provided Administrative Scale estimates for education and health functions and proposed that estimates for functions related to other assessments would need to employ the best possible approaches.

All States and Territories apart from NSW support the proposed approaches for re-estimating Administrative Scale costs, with the latter supporting the top-down and regression analysis approaches. However, Commission staff contend that since regression analysis did not prove to be a viable method in the 1999, 2004 and 2015 Reviews, they do not see any reason why it would work in the context of the 2020 Review.

Commission staff aim to estimate Administrative Scale expenses for each category.

After education and health, their priority has been the Other Expenses, Services to Industry and Justice assessments, since they account for a high proportion of total Administrative Scale expenses (these three assessments, inclusive of Schools Education and Health, together accounted for approximately 84 per cent of total Administrative Scale expenses in 2016-17¹⁶). Given that the estimation of Administrative Scale costs is resource intensive, if Commission staff cannot cover all functions, they intend to estimate Administrative Scale costs for such functions using the estimates of other functions as a guide.

States and Territories broadly agreed with the stylised structures for education and health while some, including the ACT, suggested some refinements which Commission staff intend to review. However, several States and Territories, including the ACT, questioned the reliability of estimated staffing numbers and staff classifications, the salaries and labour/non-labour costs ratio. Commission staff are relying on States and Territories to share data to improve the preliminary estimates, which the ACT has already done for the education and health functions. Commission staff intend to send data requests for information on the number of head office staff, their classifications and remuneration for each function.

The NT presented a case that the scope of Administrative Scale costs should be expanded to include the minimum level of ICT infrastructure needed to run a bureaucracy and staffing costs associated with those functions. It further added that there was specific ICT infrastructure and reporting requirements in the health sector. Commission staff have sought further evidence from the States and Territories on that issue.

State and Territory views on the education and health estimates for Administrative Scale, along with Commission staff response, are presented in Attachment A of the Draft Assessment Paper.

Commission Staff Position

Staff propose to recommend that, to the extent possible, the Commission re-estimate Administrative Scale expenses for each expense category using the bottom-up and top-down approaches.

ACT Position

The ACT supports the Commission staff recommendation. We consider that there has been a significant change in the governance environment in Australia due to rapid changes in technology and the business environment since Administrative Scale estimates were last estimated following top-down and bottom-up approaches in the 2004 Review. Hence, we consider it vital to re-estimate the Administrative Scale costs using the top-down and bottom-up approaches for all functions.

Adjustments for the Northern Territory and the Australian Capital Territory

Context

As mentioned, in the 2015 Review, the Commission adjusted Administrative Scale expenses for the ACT and the NT.

¹⁶ ACT Treasury calculation based on Table 1, p. 6 of the Draft Assessment Paper

The Commission determined that the ACT did not need to provide the average level of services in various areas – services to indigenous communities, non-urban transport, primary industry and mining, fuel and energy – since it had zero to very low needs in these areas. Hence, the ACT’s Administrative Scale expenses for the associated assessments – Services to Communities, Transport and Services to Industry - were reduced by \$10.9 million in 2016-17 (as shown in Table 2 (p. 9) of the Draft Assessment Paper).

On the other hand, the Commission recognised the NT needed to provide above average level of services in Schools Education, Health, Welfare, Housing and Services to Communities. In these areas, the NT operates a dual service delivery model catering to its indigenous and non-indigenous residents. Hence, its Administrative Scale expenses for those categories were increased by \$7.4 million in 2016-17 (as shown in Table 3 (p. 9) of the Draft Assessment Paper).

Commission staff consider it remains accurate to adjust a State or Territory’s Administrative Scale expenses where there is reliable evidence that either:

- The State or Territory has zero or very low need, indicating that it does not need to provide an average level of service; or
- The State or Territory needs to provide an above average level of service due to material disabilities.

Commission staff intend to continue the adjustments to the ACT’s Administrative Scale expenses. ABS GFS data show that the ACT has no spending on services to indigenous communities, non-urban transport, and mining and mineral resources other than fuels. The ACT spent \$5 per capita on an average between 2013-14 and 2015-16 on services to primary industries, in comparison to a national average of \$94 per capita. Commission staff propose to estimate the adjustments when they re-estimate the Administrative Scale expenses for those functions.

Regarding the adjustments made to the NT’s Administrative Scale expenses, Commission staff review of the education and health head office functions suggests that States and Territories have increased the focus on indigenous services. Most States and Territories now appear to provide services specifically catering to indigenous needs, whereas this was not the case when the Administrative Scale costs were estimated in detail in 2004. Hence, the proposed stylised head office structure for the health and education functions now include an indigenous services role. Thus, Commission staff contend that the NT may not require extra Administrative Scale expenses for indigenous services, at least in the health and education functions.

Commission staff seek evidence from States and Territories on whether they have dual service delivery models catering to indigenous and non-indigenous populations and if so, which functions have them.

They contend that if adjustments for the NT need to be continued then Commission staff will have to be convinced that the circumstances in the NT warrant extra administrative, policy and related staff in its head offices.

Commission Staff Position

Staff propose to recommend the Commission:

- Continue to adjust the ACT's scale expenses to reflect its minimal spending needs for indigenous communities, non-urban transport, primary industries, and mining and mineral resources other than fuels; and
- Decide whether to retain the adjustments for the NT based on State and Territory provided evidence about the existence of dual service delivery models.

ACT Position

The ACT supports the Commission staff recommendations.

As shown in the ABS GFS data, the ACT's per capita spending on services to indigenous communities, non-urban transport services and mining and mineral resources other than fuels is about five per cent of the national average only. Hence, the adjustment is appropriate.

Further, we consider adjustments for the NT should also be conceptually based on whether the dual service delivery model is specific to the NT due to its demographic conditions and whether other States and Territories also have such a structure. WA and QLD's views, considering their relatively higher proportion of indigenous populations in comparison to NSW, VIC and SA, will be critical on this issue.

Wages Costs Adjustment

Context

Victoria mentioned in the 2015 Review that the proportion of Administrative Scale expenses to which the Wage Costs factor applies (80 per cent) needed to be reviewed. Based on PC data on out-of-school staff and expenses, and data from the Commonwealth Departments of Health and Education, Commission staff research paper CGC 2017-06-S suggests 60 per cent may be a more appropriate proportion.

NSW challenged the Commission staff estimated ratio between staff and non-staff costs for the education and health functions using data from a number of agencies showing a labour to non-labour cost split of 75-77:25-23. Commission staff intend to review the preliminary estimate by collecting State and Territory data on labour and non-labour costs for State/Territory agencies' head offices and whole of State/Territory functions.

Commission Staff Position

Staff propose to recommend the Commission re-estimate the proportion of Administrative Scale expenses to which the Wage Costs factor should apply through the collection of State and Territory data on the proportion of wage related expenses for head office functions and whole of State/Territory services such as Treasuries, for all the Commission's categories.

ACT Position

The ACT supports the Commission staff recommendation. Data for the ACT's health and education functions' head offices show the 60 per cent figure for Wage Costs factor to be reasonably accurate. At the same time, we consider it is appropriate to adopt a final position on the Wage Costs factor once salary and non-salary cost estimates are available for all head-office functions and whole of State/Territory services.

Indexation of Administrative Scale Expenses

Context

It will not be feasible for the Commission to estimate Administrative Scale expenses using the bottom-up and top-down approaches in the context of relativity updates since it is a very resource-intensive task. This was also recognised in past reviews and subsequent updates when data driven estimates were escalated by the ABS SLGFCE deflator. The same reliable approach is proposed to be applied in future updates.

Commission Staff Position

Staff propose to recommend the Commission keep the Administrative Scale expenses up-to-date in updates following the 2020 Review by indexing them using the ABS SLGFCE deflator.

ACT Position

The ACT supports the Commission staff recommendation since we agree the ABS SLGFCE deflator is an appropriate index for the Administrative Scale expenses.

Presentation

Context

In the 2015 Review report, instead of including Administrative Scale expenses separately in each category, all Administrative Scale expenses were reported together in the Other Expenses assessment. The intention was to simplify the calculations by having one Administrative Scale assessment and avoiding the need to create Administrative Scale components in each expense category. However, Commission staff have received suggestions that it would be preferable to retain Administrative Scale expenses in each expense assessment as it would better align the category expenses data with data in ABS GFS publications.

Commission Staff Position

Staff seek State and Territory views on whether Administrative Scale expenses should all be included as a component under Other Expenses assessment or should be separately identified in each expense assessment.

ACT Position

The ACT has always supported steps which improve the transparency of assessments and which serve to show all the facets of an assessment (e.g. user charges) within the assessment itself. In that light, we support the option of separately identifying the Administrative Scale expenses in each expense assessment. A view of the total impact of the Administrative Scale disability on GST distribution, as provided currently, should also be retained for presentation purposes.

OTHER DISABILITIES

Summary

Other disabilities capture miscellaneous costs which generally impose on only one or two States. The disability is separated into three distinct categories, each with their own separate issues and assessment methods:

- National capital;
- Cross-border; and
- Native title.

The ACT contends that there are a range of additional cost imposts on the ACT Government associated with hosting the national capital that are structural and ongoing, in particular those associated with adherence to the NCP.

The ACT is conducting an audit of the delivery of its programs and services which are affected by national capital and cross-border considerations. We will provide a supplementary submission including outcomes of this audit and quantification of national capital and cross-border costs borne by the ACT.

The ACT supports the Commission staff recommendation that Native Title expenses continue to be assessed on an APC basis, noting that the expenses are small and driven by Commonwealth Government legislation, alleviating concerns regarding the principle of *Policy Neutrality* that are present when assessing on an APC basis.

However, we are concerned with the Commission staff proposal to use native title expenses as a policy neutral driver of aboriginal land rights expenses and propose that the Commission explore using the number of discrete aboriginal and Torres Strait islander languages by State and Territory as reported in the AIATSIS AUSTLANG database.

National Capital

Context

In recognition of the ACT's status as the national capital, the Commission provides a disability allowance for the additional costs imposed on the ACT as an inevitable and unavoidable consequence of its national capital role. The Commission assesses National Capital disabilities for:

- The cost of adhering to the NCP in the planning and management of the ACT, as required by the NCA, the independent Commonwealth Government body responsible for administering the NCP;
- The additional cost of using the AFP as the ACT's police force; and
- The additional cost of maintenance of over-provisioned roads as a result of the NCP.

The allowance for the additional cost of road maintenance is due to cease from the 2019 Update.

The National Capital disability allowances are the culmination of the Commission's evaluation of numerous individual elements for which the ACT has sought recognition over the course of all Reviews since the ACT was integrated into the HFE system.

They are given in accordance with the *Australian Capital Territory (Self Government) Act 1988*, which establishes the intention of the Commonwealth Parliament to avoid the ACT community incurring costs arising from national capital influences. These costs, by implication, should be shared by the entire Australian population. This intent is supported by section 5 of the *Commonwealth Grants Commission Act 1973*.

The National Capital disability redistributed \$25 million, or \$70 per capita in GST to the ACT in the 2018 Update.

Commission Staff Position

Commission staff, in Draft Assessment Paper 2018-01/25-S, propose to discontinue all national capital planning allowances unless the ACT can provide a case for their ongoing provision and retain only the National Capital disability for use of the AFP in the 2020 Review. Commission staff further argue that the roads disability should still cease from the 2019 Update and they do not consider it to be an issue for the 2020 Review.

ACT Position

The ACT notes the Commission staff view that that the ACT Government should, after 29 years of self-government, be sufficiently mature to 'deal with historical legacies' associated with national capital (and cross-border) issues.

Whilst significant efforts have been made to bring greater efficiencies to ACT administration and engage on these issues, there remain a range of additional cost imposts associated with hosting the national capital that are **structural** in terms of their impact on the ACT Government costs. Far from mitigating over time, their continuation at the time of a growing ACT economy and population bring them even more to the fore.

The ACT is currently conducting an audit of the delivery of its programs and services affected by national capital (and cross-border) considerations, with a view to improved real-time consideration of these issues and data capture where they exist. This audit coincides with the Commission's 2020 Review, and we will provide the outcome of this exercise in our supplementary submission and as part of the workplace discussions in mid-August.

Our starting position, however, is that adhering to the NCP in the planning and management of the ACT remains an ongoing impost that has not substantially lessened over time and is unlikely to change in the foreseeable future. Whilst there are instances where the ACT has been able to negotiate acceptable planning outcomes with the NCA, the ACT continues to bear significant ongoing costs as a result of its interactions with the NCA.

Following our review, we will provide the Commission with information in areas such as:

- The impact of the dual planning system;
- Unavoidable costs associated with open space requirements, the influence of the Y-plan, building height restrictions, designated areas and special requirements (including continuing road restrictions); and
- The impacts on territory planning of NCA control over crown land.

The ACT agrees with the Commission staff recommendation to retain the national capital disability in relation to the ACT's use of the AFP, and is reviewing the methodology/formula used to calculate the disability in light of the time that has elapsed since its last consideration.

Cross-border

Context

The Cross-border disability assessment is designed to capture the cost to each State and Territory of residents of other States and Territories using its government services. The Cross-border disability is of particular importance to the ACT and NSW due to the relatively large number of residents in the South-East NSW area that utilise services provided by the ACT Government. The cross-border disability only has a significant impact on the GST distribution of the ACT and NSW and only the ACT experiences a material change in its GST distribution from the disability.

Some services, specifically school education, post-secondary education, hospitals and roads, have comprehensive and reliable cross-border usage data available for use by the Commission in order to assess a Cross-border disability.

Of these services, the Commission determined in the 2015 Review that only post-secondary education required a separate cross-border allowance, as the Schools Education and Roads assessments are derived using data which already captures actual usage by out-of-State/Territory residents, while cross-border hospital costs are reimbursed through a bilateral agreement between the ACT and NSW Governments within the framework of the NHRA.

However, other services, such as recreation and culture, welfare and community health do not have reliable data from which costs may be determined. Partial data and illustrative information was used to determine that approximately seven to 10 per cent of these ACT Government services are used by cross-border residents. The Commission determined that seven to 10 per cent of the ACT's population is equal to approximately 30 per cent of the population of NSW SA2s within a one hour drive of Canberra.

On this basis, the Commission adds 30 per cent of the population of NSW SA2s within a one hour drive of Canberra to the ACT's population and subtracts an equal amount from NSW's population.

As the GST is distributed on the basis of State and Territory populations, weighted by the annually calculated relativities, this has the effect of increasing the ACT's GST share at the expense of NSW's. This process is known as the general method.

The 2018 Update redistributed \$46 million, or \$110 per capita in GST to the ACT from the Cross-border disability.

Commission Staff Position

In the Draft Assessment Paper 2018-01/25-S, Commission staff have proposed to retain the 2015 Review's approach to assessing cross-border disabilities for Schools Education, Post-secondary Education, Roads and hospitals. Commission staff have also proposed to retain the cross-border disability for community health, but update the disability on the basis of new data on cross-border community health services usage by NSW residents in the ACT and by ACT residents in NSW.

For all other services however, Commission staff are proposing to cease assessing a cross-border disability unless the ACT can provide evidence of significant cross-border use of services and how this usage translates into identifiable annual costs for the ACT Government. In effect, the Commission staff are proposing to only assess cross-border allowances for services that have reliable and comprehensive data demonstrating significant cross-border use.

Given that schools education, hospitals and roads do not have separate cross-border disabilities, this would amount to the Commission only assessing cross-border disabilities for community health and post-secondary education.

ACT Position

Cross-border remains an issue of major importance for the ACT. We seek to continue to play a responsible role in the region recognising that, in public policy terms, it is important that we do so. We are now regarded as the main service centre for the South-East NSW region. However an appropriate sharing of costs is critical to the sustainability of this approach.

The ACT supports the Commission staff recommendation to retain the cross-border disability for Schools Education, Post-secondary Education, Roads and hospitals.

The ACT supports retention of the disability for community health, and we are in the process of identifying through our policy audit the scope for providing identifiable updated data on community health services usage by NSW residents in the ACT and by ACT residents in NSW.

The ACT notes the Commission staff recommendation to cease assessing a cross-border disability for a range of other services unless the ACT can provide evidence of significant cross-border use of services and how this usage translates into identifiable annual costs for the ACT Government.

The ACT will provide in its supplementary submission details of identifiable annual cross-border costs it bears in respect of a range of other services, for the consideration of the Commission, including:

- The interaction of residual disability services in the context of full roll-out of the NDIS;
- Homelessness services – noting that the accessing of homeless services is not restricted to ACT residents and that the Census count is based on place of usual residency;
- Health costs in relation to provision of hospital services to NSW residents – to cover the capital costs of these services, which are not included in the agreement with NSW;
- Welfare services provided out of home;
- Recreation and culture services; and
- Possible new cross-border claims arising from our review.

Native Title

Context

The Native Title disability recognises the cost to States and Territories of operating the Commonwealth Government's *Native Title Act 1993* and, in the case of the NT, the cost of administering the Commonwealth Government's *Aboriginal Land Rights (Northern Territory) Act 1976*.

These two Acts recognise the rights to the traditional lands and waters of aboriginal and Torres Strait islander people. States and Territories which have large holdings of traditional aboriginal and Torres Strait islander lands and waters which are recognised under native title incur additional costs in land management and in the settlement of claims from native title holders.

The NT incurs further costs from court proceedings and compensation relating to aboriginal land rights. While all States and Territories administer aboriginal land rights, the NT is the only State or Territory which is required to do so under Commonwealth Government legislation.

Native Title redistributed \$3 million, or \$8 per capita of GST funding from the ACT in the 2018 Update.

Commission Staff Position

Commission staff, in Draft Assessment Paper 2018-01/25-S, propose to retain the 2015 Review methodology of assessing Native Title expenses on an APC basis.

Commission staff also propose to collect data on aboriginal land rights expenses from all States and Territories, not just the NT, in order to determine whether the costs for all States and Territories should be differentially assessed. Commission staff have acknowledged that a policy neutral driver of aboriginal land rights expenses would need to be identified and, in the first instance, have proposed using factors derived from native title expenses to measure the needs of each State and Territory.

ACT Position

The ACT supports the Commission staff recommendation that the Native Title disability continue to be assessed on an APC basis as they are under the 2015 Review methodology. The ACT acknowledges that the expenses assessed in the Native Title disability are very small and that, as native title claims are determined in Commonwealth courts, States and Territories have limited control over the required expenses to administer native title lands in their jurisdictions. This alleviates concerns regarding the principle of *Policy Neutrality* that are present when assessing on an APC basis.

Regarding aboriginal land rights expenditure, the ACT notes that it incurs no aboriginal land rights expenses, save for those incurred by court proceedings relating to the Wreck Bay Aboriginal Community Council under the Commonwealth Government's *Aboriginal Land Range (Jervis Bay Territory) Act 1986*. These services are provided on behalf of the Commonwealth Government on a fee-for-service basis and are not relevant to HFE.

Acknowledging this fact, the ACT is supportive of the Commission seeking State and Territory data on aboriginal land rights expenses, though we do express concern with the Commission staff proposal to use native title expenses as a policy neutral driver of aboriginal land rights expenses.

No attempt has been made to establish the case that the distribution of land rights expenses across States and Territories is the same as that for native title expenses. Therefore, the ACT considers that there is no established conceptual basis for deriving a driver for land rights expenses from native title expenses.

Aboriginal land rights are granted on the basis of the recognised dispossession of land from traditional owners during the colonial period. Therefore, States and Territories which have greater numbers of discrete aboriginal and Torres Strait islander peoples are likely to be required to provide aboriginal land rights to more groups, which would increase the cost of their administration. The ACT understands that aboriginal and Torres Strait islander languages are a key differentiator of discrete aboriginal and Torres Strait islander peoples. Thus, the ACT considers that using the number of different aboriginal and Torres Strait islander languages in each State and Territory may be a feasible means of determining the relative expenditure needs of each State and Territory with regard to aboriginal land rights.

Therefore, the ACT suggests that the Commission could examine using the AIATSIS AUSTLANG database as a determinant of the number of discrete aboriginal and Torres Strait islander peoples exist in each State and Territory. AUSTLANG is a database of known or suspected discrete aboriginal and Torres Strait island languages in Australia, including filters for individual States and Territories.

The AUSTLANG database does include a disclaimer that it is not definitive, but the ACT considers that it would still be suitable as an approximation of the number of aboriginal and Torres Strait islander peoples in each State and Territory and thus a policy neutral indicator of aboriginal land rights expenses. In order to maximise the accuracy of the information in the database, the ACT would recommend that only confirmed aboriginal and Torres Strait islander languages be used in the assessment.



ACT
Government

Chief Minister, Treasury and Economic
Development Directorate

July 2018

Table 3

Weighted Average Payroll Tax Threshold, 2015/16												
Number	Formula	Size	Data	National	NSW	VIC	QLD	WA	SA	TAS	ACT	NT
1		Extra Small	Number of organisations	19,765	6,989	5,184	2,893	2,111	1,635	508	340	105
2			Total employee expenditure (\$m)	71	22	19	13	8	6	1	2	2
3	[2]/[1]		Average employee expenditure per organisation (\$)	3,607	3,133	3,607	4,355	3,648	3,425	2,362	5,588	16,190
4		Small	Number of organisations	13,455	4,716	3,418	2,079	1,420	1,089	337	299	97
5			Total employee expenditure (\$m)	481	155	129	72	54	40	14	13	5
6	[5]/[4]		Average employee expenditure per organisation (\$)	35,779	32,846	37,683	34,776	38,169	36,915	40,059	43,813	47,423
7		Medium	Number of organisations	7,758	2,932	1,928	1,312	667	447	189	174	109
8			Total employee expenditure (\$m)	1,653	644	373	283	148	95	46	39	25
9	[8]/[7]		Average employee expenditure per organisation (\$)	213,057	219,611	193,205	215,549	221,739	213,199	243,386	226,437	230,275
10		Large	Number of organisations	6,527	2,026	1,821	904	720	495	184	211	166
11			Total employee expenditure (\$m)	11,253	3,157	3,238	1,516	1,39	959	379	33	276
12	[11]/[10]		Average employee expenditure per organisation (\$)	1,724,054	1,557,996	1,777,924	1,676,549	1,936,250	1,937,172	2,057,609	1,592,417	1,660,241

Number	Formula	Size	Data	National	NSW	VIC	QLD	WA	SA	TAS	ACT	NT
13		Extra Large	Number of organisations	1,857	574	512	292	195	137	49	55	43
14			Total employee expenditure (\$m)	25,218	7,439	7,236	4,063	2,802	1,976	602	623	477
15	[14]/[13]		Average employee expenditure per organisation (\$)	13,580,022	12,959,233	14,132,813	13,915,753	14,371,282	14,422,628	12,285,714	11,329,091	11,086,047

16		Extra Extra Large	Number of organisations	159	58	40	32	14	10	1	3	1
17			Total employee expenditure (\$m)	36,055	12,811	8,455	8,579	3,486	1,710	128	708	177
18	[17]/[16]		Average employee expenditure per organisation (\$)	226,761,006	220,886,207	211,375,000	268,100,000	249,021,429	171,040,000	127,900,000	235,933,333	177,000,000

19	[2] + [5] + [8] + [11] + [14] + [17]		Total Employee Expenses (\$m)	74,732	24,227	19,449	14,526	7,893	4,786	1,169	1,721	961
20	[19] - ([3] + [6] + [9]) - ((Table 2 4)*([1]+[4]+[7]+[10]+[13]+[16]))		Total Employee Expenses (Above Payroll Tax Threshold Only) (\$m)	41,057	12,199	10,795	9,362	4,443	2,180	319	1,053	705

Table 4

Payroll Tax Assessment Excluding Charities and Non-Profit Organisations, 2015/16											
Number	Formula	Data	National	NSW	VIC	QLD	WA	SA	TAS	ACT	NT
1		Taxable Private Sector CoE (2018U) (\$m)	436,797	149,544	104,225	78,690	64,853	22,649	5,641	5,931	5,265
2		Charity Employee Expenses Above Payroll Tax Threshold (\$m)	41,057	12,199	10,795	9,362	4,443	2,180	319	1,053	705
3	[1] – [2]	Adjusted Taxable Private Sector CoE (\$m)	395,740	137,345	93,429	69,328	60,410	20,468	5,322	4,877	4,560
4		Actual Payroll Tax Revenue (\$m)	22,568	7,900	5,357	3,692	3,477	1,108	323	422	290
5	[4]/[1]	Original Effective Tax Rate (%)	5.2	5.3	5.1	4.7	5.4	4.9	5.7	7.1	5.5
6	[4]/[3]	Adjusted Effective Tax Rate (%)	5.7	5.8	5.7	5.3	5.8	5.4	6.1	8.7	6.4
7		Population ('000)	24,010	7,681	6,098	4,813	2,551	1,707	516	400	244
8	[5 National] * [1]	Original Assessed Revenue (\$m)	22,568	7,727	5,385	4,066	3,351	1,170	291	306	272
9	[8]/[7]	Original Assessed Revenue (\$pc)	939.95	1,005.87	883.14	844.68	1,313.54	685.67	564.79	766.86	1,113.06
10	[9 National] – [9 State]	Original Total Redistribution (\$pc)	62.55	-65.92	56.81	95.27	-373.59	254.28	375.16	173.09	-173.11
11	[10] * [7]	Original Total Redistribution (\$m)	1,502	-506	346	459	-953	434	194	69	-42
12	[9 State] / [9 National]	Original Relativity		0.93446	1.06433	1.11279	0.71559	1.37085	1.66425	1.22572	0.84447

Number	Formula	Data	National	NSW	VIC	QLD	WA	SA	TAS	ACT	NT
13	[6 National] * [3]	Adjusted Assessed Revenue (\$m)	22,568	7,832	5,328	3,954	3,445	1,167	303	278	260
14	[13]/[7]	Adjusted Assessed Revenue (\$pc)	939.95	1,019.67	873.80	821.40	1,350.50	683.95	588.08	696.10	1,064.00
15	[14 National] – [14 State]	Adjusted Total Redistribution (\$pc)	70.38	-79.72	66.15	118.55	-410.55	256.00	351.87	243.85	-124.06
16	[15] * [7]	Adjusted Total Redistribution (\$m)	1,690	-612	403	571	-1,047	437	182	97	-30
17	[14 State]/[14 National]	Adjusted Relativity		0.92182	1.07571	1.14433	0.69600	1.37430	1.59834	1.35030	0.88341

18	[16] – [11]	Change in GST Redistribution (\$m)	188	-106	57	112	-94	3	-12	28	12
19	[15] – [10]	Change in GST Redistribution (\$pc)	7.84	-13.79	9.34	23.29	-36.96	1.72	-23.29	70.75	49.05
20	[17] – [12]	Change in Relativity		-0.01264	0.01138	0.03155	-0.01958	0.00345	-0.06591	0.12458	0.03893

ELASTICITY OF TAXES – GENERAL POINTS

- The CGC's concern is with tax elasticity – that is, the responsiveness of a tax base to changes in the tax rate. The tax base is generally expressed in terms of dollar values (eg: dollar value of taxable payrolls; dollar value of properties exchanged), as the taxes being assessed are normally levied on an ad valorem basis.
- The most common application of elasticities in economic theory relates to the relationship between changes in price and quantity demanded or supplied (price elasticity of demand, price elasticity of supply). In these cases, the dependent variable is a quantity, not a value.
- The impact of a change in tax rate on a tax base depends on how big or small the tax is as a proportion of the value or price – the bigger the proportion, the larger the impact on the base.
- In general, the economic incidence of a tax depends on the demand and supply curves for the good or service taxed. This means that in most cases when a tax is imposed part of the burden will fall on the consumer and part on the supplier, with an increase in price to the consumer and a fall in price to the supplier – neither bearing the full impact of the tax. The quantity of the good or service will also fall compared with the quantity exchanged prior to imposition of the tax.
- However, if supply of the good or service is completely inelastic, imposition of a tax does not change the quantity supplied, and the incidence falls entirely on the supplier ie: the supplier incurs a fall in price equal to the full amount of the tax. This is commonly what is considered to occur in the case of land tax, as land does not vary in supply (assuming land which is not actually utilised or rented out is also subject to tax) – this is referred to as capitalisation of the tax into the value of the land.
- On the other hand, if demand is completely inelastic, imposition of a tax does not change the quantity demanded, and the incidence falls entirely on the consumer ie: the consumer incurs an increase in price equal to the full amount of the tax. This is commonly what is considered to occur with a tax such as tobacco excise, where demand is quite inelastic and the tax burden falls almost entirely on the consumer.
- Stamp duty on conveyances bears some similarity to land tax, in that land is a major component of the value of property exchanged, but the supply of properties is quite elastic – suppliers can decide whether or not to list properties for sale; investors can choose whether to buy in a particular jurisdiction or another, or to put money into an alternative form of investment; owner-occupiers can decide whether or not to enter the market, continue to rent, or remain in their current property.
 - As land is a significant part of these transactions, it suggests that there will be partial capitalisation of the tax into the value of properties ie: a conveyance tax would have some dampening effect on the value of properties exchanged.
- CGC documents show that the national average effective rate of conveyance duty in 2014-15 was 4.0%. ABS data show the mean price of residential dwellings in December 2014 was \$571,700. Thus, the stamp duty on an average dwelling for CGC assessment purposes would be \$22,868 in 2014-15 terms.

- In the Leigh scenario of a 10% increase in stamp duty (\$2,287 in this example), full capitalisation into the price would cause a fall in the price to \$569,413, or a 0.4% reduction. This is considerably less than the 1-2% found in the study (and warrants further analysis).
- If the rate of stamp duty were twice as high ie: 8.0%, it would amount to \$45,736 on an average dwelling and a 10% increase would cost a further \$4,574. Full capitalisation of the increase would cause a fall in the price to \$567,126, or a 0.8% reduction (closer to the figure quoted by Leigh). Thus, the bigger the tax as a proportion of the base, the larger the impact on the base.
- The corollary of these examples of the impact of tax increases is the scenario of tax reductions, which should produce similar effects in the opposite direction ie: an increase in the total value of properties exchanged and a rise in the average price per property (as the tax capitalised into the price is lower than before the tax cut).
 - This scenario raises the prospect of tax reform increasing the size of the tax base for which the tax reduction has occurred, known as a “second order” effect, and thus giving a reduced GST share for the State undertaking reform. This was the basis for ACT’s position in the 2015 Review which advocated for an elasticity adjustment to cater for this effect.
 - Although the ACT tax reform involves a revenue-neutral approach, through offsetting increases to general rates, which are a form of broad-based land tax, this does not mean that the net effect of reform on tax bases is neutral. Shifting from more elastic to less elastic tax bases will have the effect of increasing the overall size of a State’s tax bases, and thus increasing its assessed revenue raising capacity.
- The Commission’s discussion of the elasticity issue focuses on differences between States at a point in time, rather than on the differences for any given State over time. However, given reasonable mobility of the taxed factors across jurisdictions, this approach may not be unreasonable. If different tax rates across States are substantially correlated with different per capita tax bases, after controlling for other non-policy factors which impact the size of tax bases (as the Commission attempts to do through the assessment process), then there is a case for the existence of elasticity effects which could be material.
- An alternative approach is to look at tax rate changes which have altered the relative tax rates of jurisdictions over time, and to see if these are correlated with changes in the size of assessed tax bases. This would focus on specific tax changes such as the ACT’s phasing out of conveyance duties. However, this approach has the problem of controlling for the effect of other factors which impact over time, such as economic cycles, and which may vary in their timing between States. In the case of the ACT, our tax reform program has occurred over a period of major cutbacks in the Commonwealth public service, which are likely to have impacted significantly on property sales.

Data for the Gambling Taxation Revenue Assessment

Data Source: Australian Bureau of Statistics (ABS) TableBuilder data for Census 2016
 2016 Census - Counting Persons, Place of Usual Residence (MB)
 INCP Total Personal Income (weekly), HEAP Level of Highest Educational Attainment, AGE10P Age in Ten Year Groups and SEXP Sex by STATE (UR)
 Counting: Persons Place of Usual Residence

Filters:
 Default Summation

Legend
 ACT additions to the original table from ABS TableBuilder

STATE (UR)					New South Wales Residents	NSW - Total income (\$)	Victoria Residents	Victoria - Total income (\$)	Queensland Residents	Queensland - Total income (\$)	South Australia Residents	South Australia - Total income (\$)	Western Australia Residents	Western Australia - Total income (\$)	Tasmania Residents	Tasmania - Total income (\$)	Northern Territory Residents	NT - Total income (\$)	Australian Capital Territory Residents	ACT - Total income (\$)
INCP Total Personal Income (weekly)	Average Annual Income	HEAP Level of Highest Educational Attainment	AGE10P Age in Ten Year Groups	SEXP Sex																
\$1-\$149 (\$1-\$7,799)	3,900	Not having Bachelors or higher degree	Age group 30 and above	Male	23,862	93,061,800	19,176	74,786,400	15,737	61,374,300	6,418	25,030,200	7,410	28,899,000	2,000	7,800,000	1,115	4,348,500	711	2,772,900
\$150-\$299 (\$7,800-\$15,599)	11,700	Not having Bachelors or higher degree	Age group 30 and above	Male	91,070	1,065,519,000	71,114	832,033,800	59,067	691,083,900	26,427	309,195,900	26,548	310,611,600	8,862	103,685,400	3,404	39,826,800	2,279	26,664,300
\$300-\$399 (\$15,600-\$20,799)	18,200	Not having Bachelors or higher degree	Age group 30 and above	Male	150,505	2,739,191,000	109,854	1,999,342,800	96,122	1,749,420,400	41,955	763,581,000	39,525	719,355,000	14,568	265,137,600	2,220	40,404,000	3,296	59,987,200
\$400-\$499 (\$20,800-\$25,999)	23,400	Not having Bachelors or higher degree	Age group 30 and above	Male	121,452	2,841,976,800	89,547	2,095,399,800	79,559	1,861,680,600	33,670	787,878,000	30,957	724,393,800	11,561	270,527,400	1,884	44,085,600	2,940	68,796,000
\$500-\$649 (\$26,000-\$33,799)	29,900	Not having Bachelors or higher degree	Age group 30 and above	Male	97,723	2,921,917,700	77,312	2,311,628,800	64,538	1,929,686,200	26,743	799,615,700	27,001	807,329,900	9,007	269,309,300	1,806	53,999,400	2,793	83,510,700
\$650-\$799 (\$33,800-\$41,599)	37,700	Not having Bachelors or higher degree	Age group 30 and above	Male	110,551	4,167,772,700	90,451	3,410,002,700	73,611	2,775,134,700	30,175	1,137,597,500	28,193	1,062,876,100	10,050	378,885,000	1,980	74,646,000	3,519	132,666,300
\$800-\$999 (\$41,600-\$51,999)	46,800	Not having Bachelors or higher degree	Age group 30 and above	Male	142,830	6,684,444,000	118,814	5,560,495,200	99,658	4,663,994,400	39,352	1,841,673,600	39,580	1,852,344,000	12,469	583,549,200	3,092	144,705,600	5,233	244,904,400
\$1,000-\$1,249 (\$52,000-\$64,999)	58,500	Not having Bachelors or higher degree	Age group 30 and above	Male	157,560	9,217,260,000	130,296	7,622,316,000	113,347	6,630,799,500	42,877	2,508,304,500	53,591	3,135,073,500	12,937	756,814,500	4,357	254,884,500	6,814	398,619,000
\$1,250-\$1,499 (\$65,000-\$77,999)	71,500	Not having Bachelors or higher degree	Age group 30 and above	Male	108,573	7,762,969,500	89,792	6,420,128,000	78,914	5,642,351,000	26,971	1,928,426,500	41,951	2,999,496,500	8,118	580,437,000	3,875	277,062,500	5,697	407,335,500
\$1,500-\$1,749 (\$78,000-\$90,999)	84,500	Not having Bachelors or higher degree	Age group 30 and above	Male	91,492	7,731,074,000	72,320	6,111,040,000	66,530	5,621,785,000	21,378	1,806,441,000	39,801	3,363,184,500	6,493	548,658,500	3,652	308,594,000	5,494	464,243,000
\$1,750-\$1,999 (\$91,000-\$103,999)	97,500	Not having Bachelors or higher degree	Age group 30 and above	Male	62,673	6,110,617,500	48,275	4,706,812,500	44,818	4,369,755,000	13,687	1,334,482,500	31,083	3,030,592,500	3,812	371,670,000	2,990	291,525,000	3,663	357,142,500
\$2,000-\$2,999 (\$104,000-\$155,999)	130,000	Not having Bachelors or higher degree	Age group 30 and above	Male	91,000	11,830,000,000	64,956	8,444,280,000	65,365	8,497,450,000	17,856	2,321,280,000	56,887	7,395,310,000	4,171	542,230,000	5,017	652,210,000	6,587	856,310,000
\$3,000 or more (\$156,000 or more)	156,000	Not having Bachelors or higher degree	Age group 30 and above	Male	44,283	6,908,148,000	31,161	4,861,116,000	29,671	4,628,676,000	6,950	1,084,200,000	30,241	4,717,596,000	1,696	264,576,000	2,745	428,220,000	2,404	375,024,000
Total		Not having Bachelors or higher degree	Age group 30 and above	Male	1,293,572	70,073,952,000	1,013,073	54,449,382,000	886,931	49,123,191,000	334,458	16,647,706,400	452,774	30,147,062,400	105,736	4,943,279,900	38,134	2,614,511,900	51,437	3,477,975,800

Million 1,000,000

Cells in this table have been randomly adjusted to avoid the release of confidential data. No reliance should be placed on small cells.

States (in CGC order)	NSW	Vic	Qld	WA	SA	Tas	ACT	NT
Total income (\$m)	70,073.952	54,449.382	49,123.191	30,147.062	16,647.706	4,943.280	3,477.976	2,614.512

Note In the 'Gambling Txn Assessment' sheet, the above data for total income, for 2016-17, has been considered to be for 2015-16 just to show an indicative gambling taxation assessment using the ACT's approach.
 Reason: State gambling tax revenue data is not available beyond 2015-16 and indexation to non-census years is dependent on ABS advice.

Indicative Gambling Taxation Revenue Assessment

Populations (from 2018 update Report) ('000)

	NSW	Vic	Qld	WA	SA	Tas	ACT	NT	Aus
2014-15	7 573	5 966	4 753	2 533	1 694	514	393	243	23 670
2015-16	7 681	6 098	4 813	2 551	1 707	516	400	244	24 010
2016-17	7 798	6 244	4 884	2 568	1 717	519	406	245	24 381

Population Shares (from 2018 update Report) (%)

	NSW	Vic	Qld	WA	SA	Tas	ACT	NT	Aus
2014-15	31.995%	25.206%	20.081%	10.702%	7.157%	2.173%	1.659%	1.028%	100.000%
2015-16	32.452%	25.761%	20.335%	10.777%	7.210%	2.180%	1.688%	1.033%	101.437%
2016-17	32.944%	26.381%	20.633%	10.848%	7.254%	2.193%	1.717%	1.035%	103.005%

Total Personal Income of males aged 30 and above and not having a Bachelors or higher degree (\$m)

	NSW	Vic	Qld	WA	SA	Tas	ACT	NT	Aus
2015-16	70073.952	54449.382	49123.191	30147.0624	16647.7064	4943.2799	3477.9758	2614.5119	231477.061
2016-17									

Gambling Tax Collected (\$m) Source: ABS

	NSW	Vic	Qld	WA	SA	Tas	ACT	NT	Aus
2014-15	2067	1781	1077	231	383	95	52	68	5754
2015-16	2250	1834	1136	226	384	97	51	73	6051
2016-17									

Average tax rate 2.6141%

Assessed Revenues of States and Territories (\$m)

	NSW	Vic	Qld	WA	SA	Tas	ACT	NT	Aus
2015-16	1831.8	1423.4	1284.1	788.1	435.2	129.2	90.9	68.3	6051.0

Assessed Revenue per Capita

	NSW	Vic	Qld	WA	SA	Tas	ACT	NT	Aus
2015-16	238.47	233.43	266.79	308.93	254.99	250.39	227.53	279.64	252.02

Assessed to Average Ratio

	NSW	Vic	Qld	WA	SA	Tas	ACT	NT	Aus
2015-16	0.94624	0.92623	1.05859	1.22582	1.01180	0.99354	0.90284	1.10960	1.00000

Assessed Difference (\$pc)

	NSW	Vic	Qld	WA	SA	Tas	ACT	NT	Aus
2015-16	13.5498	18.5922	-14.7656	-56.9108	-2.9740	1.6292	24.4875	-27.6222	0.0000

Distribution from EPC (\$m)

	NSW	Vic	Qld	WA	SA	Tas	ACT	NT	Redistribution
2015-16	104.081	113.368	-71.071	-145.177	-5.076	0.841	9.785	-6.751	228.075

Calculations using \$208,000 as the average annual salary of the highest bracket

	NSW	Vic	Qld	WA	SA	Tas	ACT	NT	Aus
Total Personal Income (\$m)	72376.668	56069.754	50666.083	31719.5944	17009.1064	5031.4719	3602.9838	2757.2519	239232.913
Change in revenue capacity (\$m)	2302.716	1620.372	1542.892	1572.532	361.4	88.192	125.008	142.74	7755.852
Assessed Difference for 2015-16 (\$)	13.70	19.44	-14.22	-62.49	-0.06	5.42	23.95	-33.33	0
Redistribution impact (\$)	0.15	0.85	0.54	-5.58	2.91	3.80	-0.54	-5.71	NA