



Executive summary

Horizontal fiscal equalisation and the distribution of GST

This report presents the Commission's recommendations from its 2021 Update for the distribution of the GST pool among the States and Territories (States) in 2021-22. This provides States the capacity to deliver services at a similar level (referred to as horizontal fiscal equalisation). It takes account of States' different abilities to raise revenue and their different costs of service provision. The GST pool comprises GST revenue and the top-up payment, which is \$600 million in 2021-22.

Drivers of revenue differences include mineral royalties, land values and property transactions, and payroll taxes. States also receive different levels of Commonwealth payments. Costs can vary by State for a range of reasons, including sociodemographic characteristics, wage pressures, population dispersion or density, and rates of population growth.

The Commission finalised its 5-yearly review of the methods for quantifying the relative fiscal requirements of the States in February 2020 (2020 Review). The 2021 Update applied the methods from the 2020 Review and assessed the changes in States' relative GST requirements over 2017-18, 2018-19 and 2019-20. The rolling 3-year assessment period was updated with the addition of the latest year for which data were available (2019-20).

Changes in States' relative GST requirements, as outlined in this update, can be driven by changes in States' *circumstances* (such as increased iron ore royalties, growth in the value of property transfers, growth in a State's share of Commonwealth payments); or *data revisions* (such as improved data on the value of taxable payrolls).

Transition to new equalisation arrangements

Under legislated changes to equalisation arrangements, 2021-22 will be the first year in a 6-year transition away from distributing the GST pool based solely on the Commission's assessment of States' relative fiscal capacities.¹ Over these 6 years, the Commission's assessment will be adjusted to new arrangements where no State will have a per capita GST share lower than the fiscally stronger of New South Wales or Victoria. The transition will be completed in 2026-27.

The GST relativities for 2021-22 to 2025-26 will be blends of the previous approach (providing States with the same ability to provide services) and the new approach (ensuring no State has a per capita GST share less than the lower of New South Wales or Victoria). For 2021-22, the GST relativities are a weighted average of the former (5/6ths) and the latter (1/6th).

The biggest effect of the transition to the new arrangements in this update was to increase Western Australia's GST distribution by \$629 million, partially offsetting other developments, such as strong growth in iron ore royalties, which reduced its relative GST requirement. Under the new arrangements, the Commonwealth will make supplementary payments outside the GST pool to Western Australia to give it an outcome equivalent to a relativity of 0.70.² This is the third year of this approach. From 2022-23, any such payment to a State will be funded from within the GST pool. The transition includes a 'no worse off' guarantee to ensure that no State receives less GST than it would have received in the absence of the new arrangements. The guarantee starts in 2021-22 and runs until 2026-27. Any 'no worse off' amounts will be calculated in accordance with the legislation and funded by the Commonwealth.

¹ *Treasury Laws Amendment (Making sure every State and Territory gets their Fair Share of GST) Act 2018.*

² A relativity is a per capita weight calculated by the Commission. It is used to allocate States' shares of the GST pool.



Overview of the 2021 Update

The table below shows the impact of the recommended changes in this update on the State distribution of the estimated GST pool from 2020-21 to 2021-22. The change between years includes the impact of changes in States' circumstances, data revisions and the introduction of the new arrangements.

Change in distribution of GST from 2020-21 to 2021-22

	NSW	Vic	Qld	WA	SA	Tas	ACT	NT	Total
	\$m	\$m	\$m	\$m	\$m	\$m	\$m	\$m	\$m
Estimated 2020-21 distribution	18,453	15,876	13,387	2,941	5,906	2,530	1,222	2,835	63,150
Estimated 2021-22 distribution	20,347	16,220	14,411	2,918	6,207	2,783	1,310	2,984	67,180
Change (\$m)	1,894	344	1,023	-23	301	253	89	149	4,030
Change (\$pc)	232	51	196	-9	170	464	205	626	156

Note: The final amount of the GST pool will be determined by the Commonwealth of Australia's Final Budget Outcome 2020-21.

Source: Commission calculation.

The main driver of change in States' GST shares in this update was the strong growth in the value of mining production in Western Australia, principally due to historically high iron ore prices. Given the concentration of iron ore deposits in Western Australia, this substantially bolstered its capacity to raise revenue through mining royalties, reducing its GST share and increasing those of the other States. In the case of the Northern Territory, this impact was offset by growth in royalties from other minerals. Overall, the boost in iron ore royalties was shared across all States. For Western Australia, the rise in the value of iron ore production may have a range of flow on effects; for example, a possible increase in property values and capital investment, which would have further impacts on its relative GST pool requirements over time.

The consequences of the COVID-19 pandemic on States' revenue and expenses had little direct effect on this update. This is because the pandemic affected only the last few months of the Commission's 3 assessment years (2017-18 to 2019-20).³ State budget papers indicated that States expect to see the largest budget effect of the pandemic in 2020-21, and that year will enter the Commission's assessment period in its 2022 Update.

The estimated impact of the recommendations in the 2021 Update on States' GST relativities and their share of the GST pool in 2021-22, compared with 2020-21, is outlined in the table below.

GST relativities and State shares of the GST pool, 2020-21 and 2021-22

	NSW	Vic	Qld	WA	SA	Tas	ACT	NT	Total
Relativities 2020-21	0.91808	0.95992	1.04907	0.44970	1.35765	1.89742	1.15112	4.76893	1.00000
Relativities 2021-22	0.95617	0.92335	1.05918	0.41967	1.34719	1.96067	1.16266	4.79985	1.00000
	%	%	%	%	%	%	%	%	%
Share in 2020-21	29.2	25.1	21.2	4.7	9.4	4.0	1.9	4.5	100.0
Share in 2021-22	30.3	24.1	21.5	4.3	9.2	4.1	2.0	4.4	100.0
Population share in 2021-22	31.7	26.1	20.3	10.4	6.9	2.1	1.7	0.9	100.0

Source: Commission calculation.

³ However, the Commission consulted with States on COVID-19 and this will inform its assessments in future years.



Key drivers of change in each State

Compared with 2020-21, **Victoria**, **Western Australia** and **South Australia** will have a reduced requirement (in relative terms) for GST distribution in 2021-22. Strong property transfer values over the assessment period increased the revenue raising capacity of **Victoria**. This influence was compounded by Victoria's below average expense needs and data revisions that increased its assessed capacity to raise payroll tax.⁴ The strong growth in iron ore royalties was the main driver of **Western Australia's** declining GST requirement in this update. **South Australia** experienced a small reduction in its GST requirement, mainly due to above national average growth in property sales and taxable payrolls, and data revisions in the wage costs assessment.

Major drivers of change in GST distribution, 2020-21 to 2021-22

	NSW	Vic	Qld	WA	SA	Tas	ACT	NT	Redist
	\$m	\$m	\$m	\$m	\$m	\$m	\$m	\$m	\$m
Changes in fiscal capacities									
Changes in mining	499	389	75	-1,061	59	28	26	-16	1,077
Changes in property sales	387	-210	53	-59	-122	-48	5	-6	445
Changes in capital requirements	-187	-46	84	196	19	-1	-33	-33	300
Changes in taxable land values	-206	-33	97	94	31	11	6	0	238
Growth in expenses ⁴	52	-194	12	57	-13	20	-19	85	226
Changes in Commonwealth payments	77	58	-92	-72	31	1	-8	6	173
Other revenue effects (a)	213	-248	49	-67	-2	2	38	15	317
Other expense effects (a)	143	-221	-36	67	-18	87	7	-29	304
Total change in fiscal capacities	978	-507	243	-846	-13	100	22	23	1,366
New arrangements	-218	-179	-142	629	-51	-17	-12	-11	629
Change in pool and population	1,134	1,029	922	194	365	170	79	138	(b) 4,030
Total change in GST	1,894	344	1,023	-23	301	253	89	149	(b) 4,030

(a) The other revenue and expense effects largely reflect revisions to data and other changes in State circumstances. See the discussion in Chapters 2 to 4 for details of the other revenue and expense effects.

(b) Total increase in GST and top-up payment pool.

Source: Commission calculation.

The other States experienced an increased requirement for distribution of the GST pool in this update. A decrease in **New South Wales'** share of property sales increased its GST requirements. **Queensland's** increase was mainly due to below average growth of taxable land values and property sales, and higher investment requirements. These changes were partly offset by downward revisions to natural disaster relief expenses. **Tasmania's** increased GST distribution mainly reflected an increase in its relative wage costs, and its above average expense needs.⁴ These influences were partly offset by above national average growth in property sales. The **ACT's** share of the GST pool increased because of below average growth in taxable payrolls, as well as revisions to payrolls data. Revisions to natural disaster relief expenses also contributed to the **ACT's** relative increase in GST requirements. Partially offsetting this was the impact of the **ACT's** below average expense needs.

⁴ The reduction in GST revenue in 2019-20, along with high growth in States' spending, has meant that States with expense needs below average (such as Victoria and the ACT) were assessed as requiring a lower share of the GST pool than otherwise. States with expense needs above average (such as the Northern Territory and Tasmania) were assessed as requiring a larger share of the GST pool than otherwise. This is because the proportion of the GST pool required to enable States to cover their assessed expenses and equalise their fiscal capacities increased, with the result that less can be distributed on an equal per capita basis.



The **Northern Territory's** increased requirement for GST distribution was mainly driven by its above average expense needs.⁴

For all States other than **Western Australia**, strong growth in the value of mining production in **Western Australia** led to a reduction in their relative ability to raise mining revenue. This contributed to increasing their relative GST shares. For **Victoria** and **South Australia**, this partially offset the other factors that reduced their shares. For **New South Wales, Queensland, Tasmania** and the **ACT**, this accentuated growth in their GST shares. In the case of the **Northern Territory**, the impact on its relative ability to raise mining revenue was offset by growth in the value of other minerals produced in the Northern Territory.

For more information, see the 2021 Update report