ACT Government
Chief Minister, Treasury and Economic Development

Our ref: *2014/11828*
Your ref: *Secretary@cgc.gov.au*

Mr John Spasojevic
Secretary
Commonwealth Grants Commission
CANBERRA ACT 2600

Dear Secretary

## ACT RESPONSE TO 2015 REVIEW: SIGNIFICANT CHANGES SINCE THE DRAFT REPORT – Commission Position Paper CGC 2014 -04

I am writing to provide you with a copy of the above submission in response to the Position Paper issued by the Commission via email dated 1 December 2014 with a response date of 29 December 2014.

Our submission provides responses on the full range of matters canvassed in the paper and builds on a number of responses outlined in the ACT's earlier Final Submission forwarded separately to the Commission on 22 September 2014.

Of particular note in this response is a proposal by the ACT in respect of Western Australia's argument for an alternative approach to contemporaneity of the assessments. The ACT considers this proposal would be better dealt with through the proposed rolling program, given the short timeframe and the likely significant impact of adopting the type of approach suggested by Western Australia.

To the extent we are able, given the very limited time for response, we have commented on the Health Substitutability report issued by Commission staff on 18 December 2014. Although the issues relating to substitutability were previously canvassed by staff, the report has also introduced a major change to the methodology for calculating economic environment factors in the Health assessment. The impact of this change is likely to involve a loss to the ACT of around $100m in GST compared with the position indicated in the Draft Report. States had been given no warning that such a critical change in approach, as distinct from review of placeholders, was under consideration. We believe that such a significant late change, with minimal opportunity for States to respond, is unacceptable and must be reassessed by the Commission.

Finally, we have also included in this submission our response to a request from Commission staff for comment on issues relating to the National Education Reform Agreement raised by Queensland, and comments on the assessment of the National Disability Insurance Scheme in light of recent developments in relation to drawdowns of the DisabilityCare Australia Fund.

Should you wish to discuss this submission please contact Doug Miller on 6205 4079 in the first instance.

Yours sincerely

Karen Doran
Executive Director
Economic & Financial Group
Chief Minister, Treasury & Economic Development Directorate
ACT Government

23 December 2014

ACT Government

**AUSTRALIAN CAPITAL TERRITORY**

**2015 Methodology Review**

**ACT Comments on Commission Position Paper**

**CGC 2014-04 Significant Changes since the Draft Report**

**December 2014**

**Chief Minister, Treasury and**
**Economic Development Directorate**

## INTRODUCTION

The ACT acknowledges that the terms of reference (ToR) for the 2015 Review asked the Commission to consult further with States and Territories on significant changes following consultation on the draft report issued in August 2014.

While we welcome the opportunity to comment, the position paper issued to the States and Territories on Monday 1 December 2014 did not provide sufficient clarity for the ACT to fully understand the changes and the reasons for them.

We subsequently forwarded to the Commission staff a series of questions in advance of finalising our comments for this Submission. Their prompt response to the issues raised did not help our understanding or offer the clarity we were seeking (see <u>Attachment A</u>). This in our view implied that most of what was presented was intractable at this late stage of the Review.

Hence, we have some difficulty comprehending why the Commission should still be considering Western Australia's arguments for alternative consideration to the approach to contemporaneity of the assessments.

Some of what is asked by the Commission for the ACT to respond to in such a short timeframe is at odds with other methodological issues at play. The contemporaneity arguments are matters of principle which at this late stage of the Review are too significant a change to contemplate introducing for the 2015 Review.

Indeed, they are matters best flagged in the Final Report as broader areas for potential reform to the application of the horizontal fiscal equalisation principle as part of the White Paper processes underway. More specifically, they could be identified as a priority area under a rolling review program flagged by the ACT in earlier submissions.

Finally, the comments above reflect the complexities and time constraints on all parties in this less than satisfactory reduced 2015 Review.

## SUMMARY

The ACT position is summarised below.

### Contemporaneity and Mining Revenue Assessment

<u>Commission Position:</u>

- During our consultations we have also been asked to consider a more contemporaneous assessment, in particular of mining royalty revenue. We include this issue in this paper to invite State views to inform our decision making.

<u>ACT Position:</u>

- The ACT <u>does not support</u> any move to a more contemporaneous assessment in the 2015 Review.

**Mining Related Expenditure**

Commission Position:

- We intend to introduce assessments of expenditure related to the planning and regulation of investment projects and capital grants to local governments relating to community development and amenities, and culture and recreation.

ACT Position:

- The ACT supports the introduction of a separate assessment of expenses relating to the planning and regulation of investment projects generally, subject to assurance as to the reliability and accuracy of the State provided data.
- The ACT does not support the introduction of a separate assessment of expenses on capital grants to local governments for community development and amenities.

**Health Assessment**

Commission Position:

- In the Health assessment, we intend to standardise for SES and age in the calculation of the economic environment factors. Consultant reports on the impact of private provision on State services will be sent to States as soon as they are available.

ACT Position:

- The ACT supports standardisation of the economic environment factors for SES and age.
- On substitutability factors, the ACT:
    - Supports assessment of an economic environment factor for admitted patient services.
    - Supports an estimate of 45% for substitutability between ED and GP services.
    - Supports an estimate of 45-50% for substitutability between public outpatient and private specialist services.
    - Supports an estimate of 75% for substitutability between community health and GP services.
- On the CGC staff proposal to alter the method for calculation of economic environment factors, the ACT has serious reservations and proposes that the Commission return to the approach taken in the Draft Report.

**Welfare Assessment**

Commission Position:

- In the Other general welfare component, we intend to use the relative proportions of the population in the bottom SEIFI quintile, adjusted for changes in the level of social disadvantage in each State between the 2006 and 2011 Censuses. This is measured by the changes in the relative proportions of Health Care Card holders in each State.

ACT Position:

- The ACT supports the assessment of general welfare expenses using the relative proportions of State populations in the bottom SEIFI quintile, adjusted for changes in the relative proportions of Health Care Card holders in each State.

**Regional Cost Gradient**

Commission Position

- We intend to calculate a general regional cost gradient (calculated as the simple average of the revised schools and police gradients) for extrapolation to other categories where a regional costs disability is assessed. The gradient derived from ACARA data will continue to be used for Schools education and the police gradient for Justice.

ACT Position:

- The ACT is not opposed to the application of a general regional cost gradient based on the simple average of the revised schools and police gradients.

**Urban Transport Infrastructure Assessment**

Commission Position:

- In the Transport infrastructure assessment, we intend to estimate assessed investment using a simple city population based model.

ACT Position:

- The ACT does not support the estimation of assessed investment in urban transport infrastructure using a simple city population based model. We urge the Commission to return to the assessment model proposed in the Draft Report, with a 50% discount.

**Nationally Significant Infrastructure Projects**

Commission Position

- We intend to assess national needs in relation to roads and rail infrastructure, based on the distribution of 50% of the Commonwealth payments made for on-network road and rail projects. The advice of the Department of Infrastructure and Regional Development will be sought to determine relevant projects. No other needs of national significance will be assessed, unless instructed by ToR, because the Commission is not able to develop a suitable framework for identifying such needs reliably.

ACT Position:

- The ACT supports the equal treatment of Commonwealth payments for road and rail infrastructure projects in assessments.

- The ACT does not support a 50% discount of National Network infrastructure payments, except where specifically provided for in the Terms of Reference. A maximum discount of 25% should be applied to Commonwealth payments for such projects.

## OTHER ISSUES

On two other key issues, one recently canvassed by Commission staff (NERA) and one previously raised by the ACT but not addressed in the Position Paper (NDIS), the ACT position is summarised below.

### National Education Reform Agreement (NERA)

Commission Questions

- In its submission, Queensland said that given the changes to NERA funding announced in the 2014-15 Budget, the various commitments made by States under the original agreement are now irrelevant, and if States choose to implement changes to their schools funding models despite the withdrawal of Commonwealth commitments this should be considered a State policy choice.
- In light of the changes announced in the 2014-15 Budget, we would like State views on whether States that have agreed to implement new funding models consider the agreements binding, and do States consider they are bound to allocate Commonwealth funding in a manner consistent with the student resource standard (SRS)?

ACT Response

- The ACT's view is that the NERA effectively remains in place until the end of the 2017 school year, that the bilateral agreements reached by signatory States under NERA are still relevant and that the proposed approach of the Commission to State-funded expenses is based on an average of States' actual funding arrangements, not directly on the SRS.

### National Disability Insurance Scheme (NDIS)

Commission Position

- The Commission has not stated a revised position on NDIS. However, developments in relation to State drawdowns of the DisabilityCare Australia Fund (Medicare Levy surcharge) require a reconsideration of its position as stated in the Draft Report.

ACT Position

- The ACT considers that the latest developments reinforce our proposal that an actual per capita approach be adopted in the assessment of all expenses and revenue relating to the transition phase of NDIS.

## ISSUES

### Mining Revenue assessment

The ACT understands Western Australia has stated that with a major fall forecast for iron ore royalties, using average royalties for 2011-12 to 2013-14 as the basis of the 2015-16 GST distribution would be inappropriate:

- Instead, it has suggested that a distribution based on prospective 2015-16 conditions would be preferable.

We argue that the supporting principles for the development of assessment methods for the 2015 Review have already been agreed:

- A contemporaneity supporting principle which means that, bearing in mind the objective and other supporting principles such as policy neutrality and practicality, the distribution of GST provided to States in a year should reflect State circumstances in that year as far as possible.

This implies that the current 3 year lagged assessment is, at least in most circumstances, the most reliable practical approach to providing a reasonable estimate of State circumstances in the application year.

As acknowledged in the June 2014 Draft Report, the Commission, in setting out their preliminary views made reference to the limited exception to this principle, essentially in the case of backcasting major changes in Commonwealth-State financial arrangements, only where the change is reliably known.

Indeed, the Draft Report noted the considerable difficulties in extending this approach beyond such cases.

The ACT does not consider that State, or independent, forecasts of revenues in the application year, for example for royalties, are sufficiently reliable for the Commission to use as the basis of the GST distribution:

- Past errors in forecasts have been significant and attracted national media attention.

We agree such an approach raises a range of issues, including that it would almost certainly require consequent GST adjustments in future to compensate for errors which could itself then undermine the contemporaneity of future years' GST distributions.

The ACT has already advised the Commission twice we will not support any decision to move in this direction for the 2015 Review.

Conceptually, while we agree there is always scope post the 2015 Review to examine other options to smooth or to otherwise ameliorate the impact of expected major changes in State circumstances we are not in a position to develop such a response in the time restriction placed on us.

We urge the Commission to maintain the agreed general approach in this methodology review.

However, the Commission is quite within its bounds to include a forward looking commentary on the guiding principle of horizontal fiscal equalisation in the context of a changing Federal/State environment within the ToR released for the White Papers on Federalism and National Tax Reform. The ACT would welcome this development.

**Mining Related Expenditure**

Planning and Regulation of Investment Projects

The ACT accepts that there is a conceptual case for including a disability reflecting the additional planning and regulation costs incurred by States to facilitate investment projects. We assume that this component will be separated from the current broader assessment of regulatory expenses.

However, such a disability must be applied to all investment projects, regardless of industry sector. We have consistently maintained the view that investment related to mining projects is not qualitatively different from investment related to other forms of economic development and should not be treated as a special case.

Also, we are not convinced of the reliability and accuracy of the State provided data for the Draft Report and have some concerns that the Commission will continue to simply index the quantum in future years.

Those concerns are underlined by the inability of the ACT Administration, after several attempts, to clearly identify with any accuracy the additional planning and regulation costs incurred to facilitate investment projects. This of course was also partly due to the influence of the National Capital Plan.

The ACT accepts that, if the Commission were to persevere, then State shares of private non-dwelling construction expenditure are likely to be a more accurate indicator of costs, rather than the more general indicator of population growth.

Capital Grants to Local Government

The ACT does not accept that there is a case to include a disability to reflect additional costs incurred by States to support local government infrastructure provision relating to community development and amenities.

The Draft Report gave a quite comprehensive treatment of this issue, which said that part of these State expenses could be regarded as investment, rather than recurrent expenditure, and so related to population growth, rather than being assessed on population share.

While we accept the logic of the above principle, Table 20 of Attachment 15 to the Draft Report (p.281) shows that capital grants are only “a very small part of State spending” and the Draft Report concluded that they did not warrant a separate assessment. Capital grants represented about 7.6% of community development and community amenities expenses in 2012-13, or about $194 million. However, Table 20 also shows figures for Queensland that are radically different from other States. This casts doubt on the reliability and fitness for purpose of the data being used for the proposed assessment.

In any case, this table shows that such an assessment would redistribute no more than $8 per capita for any State, and thus is not material when considered alone. We support the Commission’s previous conclusion that a separate assessment is not warranted.

**Health Assessment**

The ACT supports the Commission’s intention to maintain the Draft Report proposal for a direct approach based on administrative data on State provided services, with economic environment factors used to reflect the effect of private provision on State provided services.

<u>Substitutability between Public and Private Services</u>

The ACT’s views on the consultants’ reports on the issue of substitutability and on the CGC staff view on those reports follow. They also reflect our views as forwarded earlier to Commission staff.

We have reviewed the two reports and consider that they make a useful contribution to the consideration of key issues relating to the impact of private services on the demand for public services in the various components of the health system, specifically, admitted patients, emergency departments, outpatients and community health.

We note that there are some key areas of agreement between the two reports, namely:

- Consideration should be given to the impact of private services for admitted patients on the demand for public hospital services. This is not currently taken into account by the Commission, except in so far as demand for public hospital services is influenced by remoteness;

- Results of the ABS Patient Experiences Survey are not reliable for the purpose of estimating substitutability for emergency department services; and

- Substitutability of outpatient services needs to take account of bulk billing rates, as price is a substantive constraint on actual demand.

We also note that there is a difference between the reports in relation to the substitutability of community health services.

In our short submission on issues arising from the Heads of Treasuries meetings with the Commission (see attached extract at Attachment B), we made the distinction between the availability of private sector services and their substitutability for public sector services, saying that availability equated to the ratio of assessed services to actual (raw economic environment factor) in the Commission's Direct Model of assessment, with the substitutability factor then being applied to produce the weighted economic environment factor.

We support the Commission's approach of assessing substitutability as a common factor applying to expenditure across all jurisdictions, and assessing the availability of private services on a relative basis, State-by-State. The ratio of actual bulk-billed benefits to assessed bulk-billed benefits captures the relative impact between States of the availability of private services on public sector demand.

The ACT considers that the provision of clear definitions of the terms "substitutability" and "economic environment factor" would assist understanding and analysis of this complex area of assessment. Our preference would be for "substitutability" to be used to refer to the clinical equivalence of types of private and public services, with "economic environment factor" being used to refer to the overall availability of clinically equivalent services in the private sector. This accords with the implied logic of the Commission's approach, which treats substitutability as a common factor across all jurisdictions and availability (the ratio of assessed to actual private services) as varying between States.

The report by James Downie uses the term "potentially substitutable" for the substitutability factor applying to these services, and then applies a ratio for availability (or "accessibility") – commonly bulk billing rates – to generate the equivalent of a weighted economic environment factor. The report by Elizabeth Savage does not make such a clear distinction, as these two elements are considered together, but by implication the substitutability factors she estimates are the equivalent of weighted economic environment factors.

The ACT's view is that the Medicare data for bulk-billed benefits by State are the most fit for purpose data for calculation of the availability of private services. While consideration could also be given to the availability of private services subject to charging, some discount would need to be applied to recognise the impact of the price constraint on demand. Given the added complexity involved in determining such a discount, we support the simpler approach of using bulk-billed private services only as the measure of availability.

The Commission methodology also explicitly takes account of socio-demographic composition factors to determine an assessed level of benefits for each State. We agree that the assessed level of benefits should take into account SES and age, as well as Indigeneity and remoteness.

What then remains to be measured is the substitutability factor, which is in essence the technical or clinical equivalence between private and public sector services. Quantification of this factor must, inevitably, be largely a matter of expert judgement, as represented by the consultants' reports and other sources such as the NSW Health Department advice on substitutability of community health services.

The above conclusions accord with the advice provided by our Health agency. In summary, the ACT's view on each of the components of health services addressed by the consultants follows:

<u>Admitted Patients</u>

- The ACT supports the proposal flagged in the Health Substitutability paper to assess an economic environment factor for admitted patient services, which would take into account substitutability of private and public services, levels of private health insurance, and actual use of private services by State.
- We note advice from staff that finalisation of this element of the assessment will not be completed until around mid-January, given the need to obtain and process data from AIHW and PHIAC.

<u>Emergency Departments</u>

- The ACT accepts the view of both consultants that the results of the ABS Patient Experiences Survey are not reliable for the purpose of estimating substitutability for emergency department services
- However, analysis of the consultants' views on substitutability needs to take account of the failure, particularly by Savage, to distinguish between technical substitutability and availability. The patient behaviour aspect addressed by Savage relates to the availability factor (actual use of GP services), rather than the technical substitutability of services. Availability is already (and better) measured by the Medicare data on bulk-billed services which is what the Commission proposes to use.
- Therefore, the key element to be drawn from the consultants' reports is the technical substitutability of services. In that context, Savage comments that: "all GPs provide services that are technically substitutable with the triage 4 and 5 services provided in EDs". The ACT considers that this measure should form the basis of the substitutability ratio for ED services.
- Downie has cast some doubt on the placeholder figure of 40% in the Draft Report, but the Nagree study he quoted appears to be too limited in scope to rely on, and it is unclear in relation to the Canadian data to what extent their system is comparable to the Australian system. The use of overseas data in this context amounts to applying an external benchmark, rather than one based on what States do, and thus is not in accord with standard Commission practice.
- The AIHW figure (which is 45% for 2012-13) is based on triage categories 4 and 5, and represents the formally agreed clinical view of the substitutability in Australia between ED and GP services (see definition of "potentially avoidable GP-type

presentations", *Australia's Health 2014*, AIHW). There is no reason why that figure should not be maintained as the substitutability factor for ED services.

Outpatients

- Savage's comments again confound technical substitutability with bulk billing rates. We agree, as indicated above, that non-bulk billed private services should not be considered in determining economic environment factors. Differences between States in usage of bulk-billed private services are best measured by the Medicare data proposed to be used by the Commission.
- Downie has also commented on bulk billing rates as "varying dramatically" between different types of services. He then proposes multiplying the number of services of each type delivered by the bulk billing rate for each service to determine a "weighted bulk billing rate". However, this procedure is not necessary, given that the Commission proposes to assess availability between States using data on bulk-billed services only. Therefore, it is only what Downie refers to as "potentially substitutability" that is relevant.
- On the issue of technical substitutability of outpatient services Savage has not nominated a figure, but her comments imply a very high level of substitutability for bulk billed services.
- Downie has stated that "non-admitted services should be considered to be 100% potentially substitutable in the vast majority of specialties" and that pathology and diagnostic imaging services "should be considered close to 100% potentially substitutable".
- Together, the comments by the two consultants on technical ("potential") substitutability suggest that a very high factor, close to 100%, should be applied. However, this ignores the link between outpatient services and previous hospital admissions. We agree that there would be limited substitutability for outpatient presentations related to a previous admission. Whether the window should be as long as 12 months is debatable – if possible, the available evidence on this issue should be reviewed. In the absence of such evidence, we would accept the 50% figure for presentations related to a previous admission and support a figure of 45-50% for the substitutable services.

Community Health

- Savage has provided only very limited and subjective comment on community health, suggesting that further investigation is required and that the level of substitutability will vary between types of services.
- Downie has commented again on bulk billing rates for community health services. As indicated above, this is already taken account of by the use of Medicare data on bulk billing rates by State.
- On the issue of technical substitutability, Downie offers the general statement that "the vast majority of community health services are available in the private sector". His comments on bulk billing rates as varying between 62% and 99% for relevant

services, and the approach he has proposed for calculating substitutability by multiplying numbers of services by bulk billing rates, suggest that his proposed 75% factor is essentially an average bulk billing rate, leaving the implication that the technical substitutability of these services is close to 100%.

- However, given the lack of reliable data for this sector and some difference of views between the consultants, we support maintaining a substitutability factor of 75% for community health services.

Change in Assessment Method

The Staff Paper on Health Substitutability issued on 18 December 2014 has taken a major step beyond what was signalled in the Draft Report and the consultants' reports by substantially revising the methodology used to calculate the economic environment factors. While potential change to the placeholders for substitutability had been identified in the Draft Report and through the consultants' reports, States had been given no warning that a critical change in approach was to occur in the calculation of the economic environment factors. These proposed changes, if accepted by the Commission, would cost the ACT around $100m in GST compared with the method proposed in the Draft Report.

The very late advice of this change leaves States with very little opportunity to analyse the approach or to respond effectively. A loss of this size, combined with likely adverse outcomes for the ACT in other major assessment categories, is not sustainable for the Territory. Accordingly, we ask that the Commission return to the approach to calculation of economic environment factors set out in the Draft Report.

**Welfare Assessment**

The ACT supports the Commission's proposal to assess general welfare expenses using the relative proportions of State populations in the bottom quintile of the SEIFI, as measured by the 2006 Census. Adjustment by the change in the relative proportions of State populations with Health Care Cards between the 2006 and 2011 Censuses appears reasonable. Adoption of the ABS's new household level index of disadvantage should occur when that is available, as part of the next Update after its release.

**Regional Cost Gradient**

The ACT has no comments on this section.

**Urban Transport Infrastructure Assessment**

We are very surprised with this late development. We have worked with the Commission during the course of this review and provided our comments on the regression based approach to this assessment and offered suggestions for improvement in our final submission. To simply walk away from it at such a late stage of the Review is disturbing.

If the Commission shares the concerns expressed by States about the quality and policy neutrality of the data and the appropriateness of the regression model used in the Draft Report, then an appropriate discount should be applied to the assessment outcome, and the model should be further tested and adjusted, as the ACT proposed in its Final Submission.

While we agree that the conceptual case that large cities require more assets per capita than small cities to deliver urban transport services has been established, the specific parameters of the model have not been firmly established. The simplified approach belatedly being proposed by the Commission is a large step backwards and should not be proceeded with.

Table 6 of the Position Paper on Assessed Investment (page 10) highlights our concerns (see adapted version of the Table attached at Attachment C). Averaging over the three assessment years, the smallest States have suffered very large losses in percentage terms as a result of application of the square of population rather than the Draft Report method: Tasmania down 53%, NT down 42% and ACT down 34%. This difference appears to be mainly driven by the removal of the intercept factor through moving to a function which goes through the origin (as indicated by the Commission's email response to Peter Cox (WA Treasury) on 4 December 2014). Not surprisingly, such a change has only a small impact on large States and a very large impact on small States. Without further justification this result is unacceptable.

The Position Paper also claims that "concerns about the sensitivity and non-policy neutrality of asset data have been reduced". From discussion with Commission staff we understand that this statement is based on the fact that the assessment model is no longer based on actual data for asset values at individual city level. This change in approach appears to have been motivated by the difficulty of obtaining reliable data at that level, and by concerns of some States about confidentiality. As a result, actual data for asset values is only used at the National level.

This simplistic approach abandons the method based on individual cities, which offered the benefits of a large data set, was consistent with the new approach to determining average policy and consistent with the assessment for urban transport operating expenses (as stated in the Draft Report, para 60, Attachment 21, p.379). What is now proposed appears to involve an abandonment of the Commission's fundamental principles, including the principle that assessments should be based on data that are reliable and fit for purpose. We now have an assessment that is barely based on data at all.

The ACT urges the Commission to revert to the method proposed in the Draft Report, with refinements of the model as appropriate, and application of a 50% discount to the assessment (based on discounting by 50% the difference between the per capita asset values estimated from the regression model and the national average per capita asset values). Given that this assessment, after allowing for a 50% discount, will redistribute about $500m in GST in one year, the Commission should consider phasing it in over three years.

**Nationally Significant Infrastructure Projects**

The ACT supports the Commission's proposal to treat Commonwealth payments for road and rail projects in the same way. This will remove the current inequity and bias against rail. Of course, decisions on equalisation must take account of whether those projects are on the National Land Transport Network or not.

As we have submitted previously, the concept of national needs as currently applied by the Commission lacks rigorous definition or means of measurement. While national needs can be equated (roughly) to whether a road or rail project is part of the national network, the application of an across-the-board 50% discount to payments for national network projects is arbitrary and lacking in any quantified evidential basis.

The problems with this assessment have been reinforced by the Commonwealth Treasurer's recent proposal to issue supplementary ToR for the Review which include application of a 50% discount to projects under the Infrastructure Growth Package announced in the 2014 Commonwealth Budget. However, the rationale for applying the 50% discount to these projects, while applying a 100% discount to payments under the Asset Recycling Fund and making no direction as to the treatment of other roads projects is unclear. When combined with the current Commission proposal to discount by 50% road and rail funding of "national significance" a combined sum of **$15 billion** in infrastructure funding will in effect, be removed from the equalisation process over the period from 2013-14 to 2018-19.

The funding listed by the Commonwealth for the 50% discount goes overwhelmingly to the two biggest States, NSW and Victoria ($7.4 billion out of a total of $9.4 billion), with no funding for the ACT or Tasmania in the list. These large infrastructure projects will inevitably draw resources and investment towards the big States and further disadvantage the fiscally weaker small States, the reverse of what fiscal equalisation is intended to achieve.

The inconsistency of the equalisation treatment of infrastructure is highlighted in the attached spreadsheet which the ACT has drawn up (<u>Attachment D</u>). Hence, the approach taken by the Commission should be directed at minimising the inequity already present in this assessment category by applying the minimum reasonable discount to the assessment. On this basis, the ACT contends that, in the absence of any method for quantifying national needs on a project-by-project basis, <u>the discount for Commonwealth payments for national network projects should be only 25%.</u>

**National Education Reform Agreement (NERA)**

Commission staff recently sought comments from States on whether those States that have agreed to implement new funding models under NERA consider the agreements binding, and whether these States consider they are bound to allocate Commonwealth funding in a manner consistent with the Schooling Resource Standard (SRS). This was in response to Queensland, which has submitted that commitments made by States under the NERA are now irrelevant and that changes to schools funding models should be considered a State policy choice.

The ACT's view is that the NERA effectively remains in place until the end of the 2017 school year, that the bilateral agreements reached by signatory States under NERA are still relevant and that these agreements collectively represent the average policy of States in relation to schools education - the five signatory States being responsible for about two-thirds of total schools education expenses. The Commission's proposed assessment approach, while quarantining the Commonwealth payments and associated expenses for disadvantage under the SRS, applies an approach to the remaining State expenses based on the average of what all States do, using the ACARA data, i.e. it is not based directly on the Commonwealth's SRS model.

The ACT also notes that the "no unwinding" requirement of the ToR for the 2015 Review specifically refers to the NERA as its authority and the Federal Treasurer has not included any change to this in his proposed Supplementary ToR issued for comments by States.

In summary, we cannot agree with the Queensland critique, either in relation to the policy being followed by States or the assessment approach proposed by the Commission.

**National Disability Insurance Scheme (NDIS)**

The treatment of State expenses during the Transition phase of NDIS was raised by the ACT as a key issue of concern in our Head of Treasury's meeting with the Commissioners on 29 October 2014. However, the Commission's Position Paper makes no reference to NDIS.

The importance of this issue has been reinforced by the Commonwealth Treasurer's proposed Supplementary ToR for the 2015 Review, which includes the following provision:

- *The treatment of state drawdowns from the DisabilityCare Australia Fund*: drawdowns from the DisabilityCare Australia Fund should have no impact on the GST relativities.

The ACT understands that the Commonwealth has based this addition to the ToR on the decision of a Senior Officials (PM&C and State/Territory First Ministers' Departments) Meeting (SOM) in May 2013 to ensure that such drawdowns have no impact on the GST relativities. The rationale for this decision was not explained in the SOM agenda paper of the time, but our assumption is that the intention was to support States as they signed participants up to NDIS, <u>reflecting differences between States</u> in the pace and timing of this process. If that assumption is correct, then it needs to be recognised that the quarantining of drawdowns is only a partial implementation of the principle, and will have no impact on the GST distribution if the Commission also quarantines the expenses associated with this revenue. A fair equalisation outcome must recognise the differences between States in the pace, and hence cost, of the transition process – this can only be achieved by treating <u>all costs and expenses</u> on an actual per capita basis.

Inclusion of this provision in the ToR also carries the implication that the drawdown provisions are not a matter of State policy choice, but a common policy determined by the Commonwealth. Moreover, as the level of drawdowns is determined by the rate at which participants are taken into the Scheme, then by implication that too is not a matter of State policy choice. The advice we have is that the rate of intake into the scheme is driven by the National Disability Insurance Agency, through their assessment processes, and not by State government agencies. This reinforces the ACT's contention that the Transition arrangements should be regarded as a national policy, not a matter of individual State policy choices.

The ACT has drawn the attention of the Commonwealth Treasury to the Commission's proposal in the Draft Report on the 2015 Review to treat any Commonwealth payments to States associated with NDIS as impacting on the GST distribution. We indicated that the proposed ToR will require the Commission to take a different approach to the draw-downs, and hence to the associated expenditure, and suggested that, before finalising the Supplementary ToR*,* Commonwealth Treasury raise the ACT's concerns with the Commission to see if any changes to the proposed wording are warranted.

**Attachments**

A. 2015 Review – Significant Changes since the Draft Report, Commission Position Paper CGC 2014-04 – ACT Questions & Commission Responses

B. ACT Submission on issues arising from the Heads of Treasuries meetings with the Commission – extract on substitutability of health services.

C. Table 6 of the Position Paper on Assessed Investment (Urban Transport Infrastructure) - adapted version.

D. Payments to Support State Infrastructure Services.

**ATTACHMENT A**

## 2015 REVIEW – SIGNIFICANT CHANGES SINCE THE DRAFT REPORT
## COMMISSION POSITION PAPER CGC 2014-04 – ACT QUESTIONS & CGC RESPONSES

**Mining Revenue Assessment**

Our previous comments on Western Australia's proposal concerning a more contemporaneous approach to assessments were couched in terms of such an approach applying across the board, to all assessment categories. From reading the comments of other States on the issue, it would appear that they also interpreted the proposal that way. However, the Commission Position Paper seems to be canvassing a limited extension of an application year based approach for mining revenue only. Can you clarify whether this is the case or not.

**Response: Paragraph 13 clearly sets out the advice it seeks from States relating to general principles etc.**

**Mining Related Expenditure**

<u>Planning and Regulation of Investment Projects</u>

The ACT Administration was not able to identify separately the additional planning and regulation costs incurred to facilitate investment projects. This of course was also partly due to the influence of the National Capital Plan. We were not convinced of the reliability and accuracy of the State provided data for the draft report.

- What has changed that facilitates consistency for its identification across jurisdictions for the future?

- Is there a reason for using State shares of private non-dwelling construction expenditure as the driver of costs, rather than, say, population growth, as used in the current investment assessment?

**Response: Paragraph 17 sets out that the Commission does not propose to gather this data in future years, rather it proposes to index the quantum.**

**Response: Interstate shares of investment projects appear more closely related to the share of private non-dwelling construction expenditure than population growth.**

<u>Capital Grants to Local Government</u>

Our first reaction was that Federal Financial Assistance Grants via State Grant Commission disbursements should reflect the increased need by Councils in these regions.

- Can you indicate the source of the data used for the expenditure on capital grants to local government for these explicit needs?

**Response: The data are sourced from ABS GFS.**

  - Is it outside the current scope of the standard budget? What States do to fund Local Government from their general government sector revenues in our opinion are not within scope of the Commission's remit?

**Response: No.**

  - Does it include data on the Western Australian government's *Royalties for Regions* program?

**Response: This is best addressed to the ABS.**

**Welfare Assessment**

- Is the ABS developing a household level index of socio economic status using 2011 Census data?
  - If not, will the Commission pursue with the ABS the desirability of doing so?

**Response: As far as we are aware, the ABS intends to develop such an index.**

**Urban Transport Infrastructure Assessment**

We are very surprised with this late development. We have worked with the Commission during the course of this review and provided our comments on the regression based approach to this assessment and offered suggestions for improvement in our final submission. To simply walk away from it at such a late stage of the Review is disturbing.

- Is there a reason for the apparent scrapping of the modelling approach using actual data to determine the relationship between city size and transport infrastructure needs?

**Response: The Commission's paper at para 32-35 sets out the proposal to simplify this assessment and rationale.**

- Is there a contradiction between an assessment based on squares of the populations of urban centres and the statement that the relationship between asset values per capita and city size is linear?

**Response: No. The earlier staff email sent on 1 September 2014 sets out the rationale.**

- Is the statement "concerns about the sensitivity and non-policy neutrality of asset data have been reduced" based on the fact that the assessment model is no longer based on actual data?

**Response: The assessment will not require asset values by city. It will use population data only.**

- Does the square of population figures in Table 5 include a discount or not?

**Response: There is no discount on either set of numbers. The Commission will determine the discount as part of its review of all discounts later in the review.**

- If the Commission is "inclined to reduce the placeholder discount of 50% adopted in the draft report", what level of reduction is envisaged?

**Response: To be determined when the Commission finalises its assessment.**

**Nationally Significant Infrastructure Projects**

- Is there any justification for the exclusion of 50% of Commonwealth payments to States for national network road and rail construction, on the basis that they relate to national needs, rather than a different percentage, say 25%?
    - Is the Commission prepared to review the available evidence to substantiate the 50% figure?

**Response: The Commission would welcome evidence from all jurisdictions which would inform its final decision.**

Federal Financial Relations

ACT Treasury

2 December 2014

**ATTACHMENT B**

**2015 METHODOLOGY REVIEW – ACT SUBMISSION ON ISSUES ARISING FROM HEADS OF TREASURIES MEETINGS WITH COMMONWEALTH GRANTS COMMISSION**

**EXTRACT ON SUBSTITUTABILITY OF HEALTH SERVICES**

**Health Services - Substitutability**

The ACT considers that separating the assessment of substitutability of health services into three categories, covering emergency department services, outpatient services and community health, is logical and appropriate. This approach recognises that the level of substitutability and the availability of evidence as to that level is likely to vary between the categories. We consider that both clinical assessment and patient experience are relevant in assessing the degree of substitutability of services – patient beliefs, and hence behaviour, are crucial, but not sufficient, as clinical decision-makers or gatekeepers play a key role in every stage of a patient journey.

The information presented in the Commission's Draft Report indicates that there is substantive evidence to support a substitutability estimate of 40-45% for emergency department services. We do not agree with an interpretation by another jurisdiction of the ABS *Patient Experiences in Australia* study which would count only the 23% of services which people thought could have been provided by a GP as substitutable, and not also the 15% of services where people thought care could not be provided only or mainly because of the time of day when care was sought. The total of these two categories should be treated as the substitutability factor; while the time of day element represents availability of the service – which is already captured in the raw economic environment factor[1]. The latter view would go close to reconciling the clinical assessment and patient experience perspectives on substitutability. We consider that the data presented at Figure 4 on p.195 of the Draft Report also provide indicative support for a fairly high degree of substitutability between ED and GP services.

In relation to outpatient services, the figure of 50% with low substitutability due to a link to a previous admission is clearly evidence-based, with a somewhat greater degree of judgement in the estimate for substitutability within the remaining 50% of services. For community health, some greater uncertainty is introduced by the use of ED data for triage

[1] The ratio of assessed services to actual in the Direct Model (raw economic environment factor) can be characterised as availability – with an adjustment then made for substitutability to produce the weighted economic environment factor. To further clarify, while availability of a given service will vary across States, substitutability of a given service should be the same across States (eg: as shown by Table 9, Draft Report, p.197).

categories 4 and 5, and by the lack of patient survey or clinical assessment data to support estimates of substitutability.

We have explored the issue of substitutability of community health services further with our Health Directorate and have not been able to identify data which provides a breakdown of public sector spending in the categories used by NSW Health. Estimates from a Local Health District within one State cannot be considered as sufficient evidence, and we would expect to see information from a number of other States before consideration could be given to its use in estimating substitutability for the community health component of the assessment.

The relative size of substitutable private services compared to total State services is of course critical to an assessment of States' health spending needs, but this is an issue both with the new model proposed by the Commission and the subtraction model adopted in the 2010 Review. Under either model, you first need to determine which services are substitutable and to what degree. Both models rely on assumptions about the level of substitutability and those assumptions in turn rest inevitably on subjective judgements. Where these judgements are supported by substantive evidence, such as consensus views of clinical experts and surveys of patient experiences, the estimates of substitutability should be considered as more robust and fit for purpose than those for which there is less substantive evidence.

The ACT is also concerned about the lack of information so far on the consultancy which the Commission has commissioned on the health substitutability issue. The results of this exercise will clearly be critical to the final position taken by the Commission, with potential to significantly alter the provisional estimates in the Draft Report. We would appreciate further information as soon as possible about the progress of the consultancy and its expected completion date, in light of the Commission's commitment to consult with States by the end of November on any significant changes to the Draft Report.

Federal Financial Relations

ACT Treasury

24 November 2014

**ATTACHMENT C**

## TABLE 6 OF THE POSITION PAPER ON ASSESSED INVESTMENT - URBAN TRANSPORT INFRASTRUCTURE

### Table 6 Assessed Investment

| | NSW | Vic | Qld | WA | SA | Tas | ACT | NT | Total |
|---|---|---|---|---|---|---|---|---|---|
| | $m | $m | $m | $m | $m | $m | $m | $m | $m |
| Draft report method no discount (A) | | | | | | | | | |
| 2010-11 | 3,064.7 | 2,703.0 | 737.5 | 504.0 | 256.7 | 10.6 | 24.2 | 6.2 | 7,307.0 |
| 2011-12 | 1,367.2 | 1,350.1 | 394.1 | 334.2 | 102.4 | 3.2 | 12.4 | 1.4 | 3,565.0 |
| 2012-13 | 1,658.2 | 1,619.2 | 731.1 | 565.7 | 205.4 | 30.1 | 47.8 | 12.5 | 4,870.0 |
| Average | 2,030.0 | 1,890.8 | 620.9 | 468.0 | 188.2 | 14.6 | 28.1 | 6.7 | 5,247.3 |
| | | | | | | | | | |
| Square of population (B) | | | | | | | | | |
| 2010-11 | 3,072.6 | 2,658.1 | 738.9 | 529.1 | 261.7 | 12.7 | 26.0 | 7.8 | 7,307.0 |
| 2011-12 | 1,380.2 | 1,322.4 | 390.0 | 348.2 | 104.6 | 3.9 | 13.7 | 1.9 | 3,565.0 |
| 2012-13 | 1,841.2 | 1,794.4 | 551.4 | 519.4 | 141.5 | 4.0 | 16.2 | 1.9 | 4,870.0 |
| Average | 2,098.0 | 1,925.0 | 560.1 | 465.6 | 169.3 | 6.9 | 18.6 | 3.9 | 5,247.3 |
| | | | | | | | | | |
| Change (B-A) | 68.0 | 34.2 | -60.8 | -2.4 | -18.9 | -7.8 | -9.5 | -2.8 | 0.0 |
| % change | 3.35% | 1.81% | -9.79% | -0.51% | -10.04% | -53.08% | -33.77% | -42.29% | 0.00% |

Note: Three year averages have not been used in the stock disabilities for either calculation but will be in the final 2015 Review assessment.

Source: Staff calculation.

**Percentages of total**

| | NSW | Vic | Qld | WA | SA | Tas | ACT | NT | Total |
|---|---|---|---|---|---|---|---|---|---|
| | $m | $m | $m | $m | $m | $m | $m | $m | $m |
| Draft report method no discount (C) | | | | | | | | | |
| 2010-11 | 41.94% | 36.99% | 10.09% | 6.90% | 3.51% | 0.15% | 0.33% | 0.08% | 100.00% |
| 2011-12 | 38.35% | 37.87% | 11.05% | 9.37% | 2.87% | 0.09% | 0.35% | 0.04% | 100.00% |
| 2012-13 | 34.05% | 33.25% | 15.01% | 11.62% | 4.22% | 0.62% | 0.98% | 0.26% | 100.00% |
| Average | 38.11% | 36.04% | 12.05% | 9.30% | 3.53% | 0.28% | 0.55% | 0.13% | 100.00% |
| | | | | | | | | | |
| Square of population (D) | | | | | | | | | |
| 2010-11 | 42.05% | 36.38% | 10.11% | 7.24% | 3.58% | 0.17% | 0.36% | 0.11% | 100.00% |
| 2011-12 | 38.72% | 37.09% | 10.94% | 9.77% | 2.93% | 0.11% | 0.38% | 0.05% | 100.00% |
| 2012-13 | 37.81% | 36.85% | 11.32% | 10.67% | 2.91% | 0.08% | 0.33% | 0.04% | 100.00% |
| Average | 39.52% | 36.77% | 10.79% | 9.22% | 3.14% | 0.12% | 0.36% | 0.07% | 100.00% |
| | | | | | | | | | |
| Change (D-C) | 1.41% | 0.74% | -1.26% | -0.07% | -0.39% | -0.16% | -0.20% | -0.06% | 0.00% |
| % change | 3.70% | 2.04% | -10.47% | -0.77% | -11.15% | -57.17% | -35.40% | -47.73% | 0.00% |

**ATTACHMENT D**

# COMMONWEALTH PAYMENTS FOR STATE INFRASTRUCTURE

| National Partnership Payments ($million) | 2013-14 | 2014-15 | 2015-16 | 2016-17 | 2017-18 | Proposed CGC Treatment | ACT Comment |
|---|---|---|---|---|---|---|---|
| **Infrastructure Investment Programme** | | | | | | | |
| Black Spot projects | 64.5 | 60.0 | 60.0 | 60.0 | 60.0 | For State roads 100% equalised (a) | |
| Bridges renewal programme | | 60.0 | 60.0 | 60.0 | 60.0 | For State roads 100% equalised (a) | |
| Heavy vehicle safety and productivity | 40.0 | 48.0 | 40.0 | 40.0 | 40.0 | 100% equalised | |
| Improving the national network | 0.8 | | | | | | |
| Investment | | | | | | | |
| Rail | 332.7 | 353.7 | 124.2 | 23.5 | 24.6 | 100% equalised | |
| Road | 4,279.6 | 3,005.9 | 3,973.4 | 5,311.6 | 2,780.0 | 50% equalised - national network | **NO** |
| Off-network projects | | | | | | | |
| Rail | 89.6 | 115.9 | 219.0 | 160.1 | 3.0 | 100% equalised | |
| Road | 404.8 | 556.4 | 354.3 | 395.4 | 222.6 | 100% equalised | |
| Supplementary | 7.5 | | | | | | |
| Roads to Recovery | 373.2 | 349.8 | 349.8 | 349.8 | 349.8 | For State roads 100% equalised (a) | |
| **Infrastructure Growth Package** | | | | | | | |
| Asset Recycling Fund | | | | | | | |
| Asset Recycling Initiative | | 335.0 | 1,278.0 | 1,285.0 | 1,007.0 | Excluded - supp. terms of reference | |
| New investments | | 201.7 | 1,010.1 | 969.2 | 519.3 | 50% equalised - supp. terms of reference | |
| Western Sydney Infrastructure Plan | | 103.0 | 210.2 | 351.6 | 530.9 | 50% equalised - supp. terms of reference | |

| | | | | | | |
|---|---|---|---|---|---|---|
| **Other Projects** | | | | | | |
| Building Australia Fund | | | | | | |
| Rail | 1,128.0 | 331.0 | 232.1 | | | 100% equalised |
| Road | 72.0 | 48.1 | | | | 100% equalised |
| Centenary of Canberra 2013 - | | | | | | |
| a gift to the national capital | | 10.0 | | | | Excluded - terms of reference |
| Community Infrastructure Grants - | | | | | | |
| Glenbrook precinct upgrade | 0.8 | | | | | 100% equalised |
| Interstate road transport | 77.0 | 77.0 | 77.0 | 77.0 | 77.0 | 100% equalised |
| Latrobe Valley economic diversification | 2.4 | 5.4 | 3.1 | | | State component 100% equalised, local component excluded. |
| Liveable communities | 9.5 | | | | | State component 100% equalised, local component excluded. |
| Local Government and Regional Development - | | | | | | |
| infrastructure employment projects | 1.6 | | | | | Excluded - local government |
| Managed motorways | 20.8 | 9.4 | | | | 100% equalised |
| Murray-Darling Basin regional economic | | | | | | |
| diversification programme | 10.0 | 32.5 | 30.5 | 24.7 | | 100% equalised |
| Townsville Convention and Entertainment Centre | 5.0 | | | | | Excluded - local government |
| **Total** | **6,919.8** | **5,702.8** | **8,021.7** | **9,107.9** | **5,674.2** | |

**Notes:**

(a) All payments for State roads equalised, but any for local roads will be excluded.