Australian Government
Commonwealth Grants Commission

2025 Methodology Review

Services to communities consultation paper

June 2023

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Overview of category

1 The services to communities assessment currently covers:

- state and territory (state) subsidies for the ongoing provision of water and wastewater services (both operating and capital subsidies)
- state subsidies for the ongoing provision of electricity services (both operating and capital subsidies) irrespective of energy source
- support for community development in discrete First Nations communities,[1] which includes co-ordinating capital works programs, managing state land rights legislation and land tenure, developing community plans, and educating community leaders about planning processes
- other community development expenses related to administration and planning including regulating land use, administering zoning laws and providing facilities for community health, recreation and culture
- expenses associated with administering environmental protection legislation and funding environmental protection measures.

2 The category currently excludes:

- concessions for electricity and water bills (for example, to pensioners and health care card holders), which are assessed in the welfare category
- regulation expenses for the electricity and water sectors, and expenses related to irrigation and other industrial uses of water, which are assessed in the services to industry category
- expenses associated with economic development, including the development of new electricity businesses, which are assessed in the services to industry category
- expenses to fund the construction of housing, industrial buildings, public utilities or any other facilities, which are assessed in the investment category
- social housing services, which are assessed in the housing category.

3 The revenue and expenses of public non-financial corporations that provide water, wastewater and electricity services are not included in the scope of state expenses (adjusted budget) considered by the Commission, on the assumption that they operate predominantly on a commercial basis.

Current assessment method – 2020 Review

4 The main drivers of expense needs in the services to communities assessment are the costs of service delivery to small, remote and First Nations communities along with state population. In the 2020 Review a reliable driver of the need for state expenses on environmental protection was not found.

[1] A discrete First Nations community is defined as a Statistical Areas Level 1, where First Nations people comprise more than 50% of the population, as measured by the latest census data.

Data used in the assessment

5 Tailored annual state data requests are used to identify state spending on water, wastewater and electricity subsidies and community development in discrete First Nations communities. Expense data from relevant Australian Bureau of Statistics' (ABS) Classification of the functions of government (COFOG-A) codes are used for other components.

6 ABS census data are used to determine the proportion of each state's population living in small communities, remote communities and discrete First Nations communities for the water, electricity and First Nations community development components.

7 For remote community electricity subsidies, the Commission requests data from states during each review. The data are used to identify the characteristics of remote communities receiving subsidies and to calculate cost weights to reflect the difference in the level of per capita subsidies for remote and very remote communities. The data sought includes expenses, revenue and subsidies, the amount of electricity supplied, number of connections, fuel type, Indigenous status of the community and geospatial information about the service area.

8 For small community water subsidies, detailed state data requested during each review are used to estimate the share of total water subsidies provided to small communities.

Category and component expenses

9 State expenses on services to communities were around $13 billion in 2021–22, representing 4.5% of total state expenditure (see Table 1). The Northern Territory spent the largest share of its state budget on services to communities and Tasmania the smallest.

Table 1 Services to communities expenses by state 2021–22

	NSW	Vic	Qld	WA	SA	Tas	ACT	NT	Total
Total expenditure ($m)	3,782	3,524	2,284	1,927	594	167	252	460	12,990
Proportion of total expenditure (%)	4.4	5.3	3.8	5.1	3.1	2.6	4.4	7.4	4.5

Source: Commission calculation.

10 State expenses on services to communities have increased from $9.2 billion in 2018–19 to around $13 billion in 2021–22 (around 41% growth) (see Table 2).

11 The highest growth has been in electricity subsidies (91%).

- Spending on electricity subsidies increased from $862 million in 2018–19 to $1.6 billion in 2021–22.
- The main reason for this growth was the inclusion of Victoria's spending on a rooftop solar program, that had previously been assessed in the services to industry category.
- Queensland, Western Australia and the Northern Territory increased their subsidies to non-remote communities between 2018–19 and 2021–22.[2]

12 However, the growth in other community development (70%) and environmental protection (24%) contributed the most to the growth in the category given their much larger expense weighting. Water subsidies declined by almost 3%.

Table 2 Total services to communities expenses 2018–19 to 2021–22

	2018-19	2019-20	2020-21	2021-22
Total expenditure ($m)	9,232	9,778	12,389	12,990
Proportion of total expenditure (%)	3.9	4.3	4.9	4.5

Source: Commission calculation.

13 The services to communities assessment currently has 7 components (see Table 3). The table shows the size of each component and the driver used by the Commission to assess states' expense needs.

[2] Tasmania ceased providing subsidies to non-remote communities in 2019–20. New South Wales and the ACT continue their policy of not providing subsidies to non-remote communities. South Australia only provides subsidies to remote communities.

Table 3 Structure of the services to communities assessment, 2021–22

Component	Component expense	Driver	Influence measured by driver
	$m		
Water subsidies	474 (4%)		
Small communities		Small communities	Recognises that costs are higher for small communities.
		Regional costs	Recognises the higher costs for small communities in outer regional and remote areas.
		Wage costs	Recognises the differences in wage costs between states.
Other		EPC	The driver of these expenses is state population.
Electricity subsidies	1,647 (13%)		
Remote communities		Remote communities	Recognises that costs are higher for remote communities.
		Regional costs	Recognises the higher costs for providing services in very remote communities.
		Wage costs	Recognises the differences in wage costs between states.
Other		EPC	The driver of these expenses is state population.
First Nations community development	301(2%)	Population in discrete First Nations communities	Recognises the higher costs of providing services in discrete First Nations communities.
		Wage costs	Recognises the differences in wage costs between states.
		Regional costs	Recognises the higher costs of providing services to remote communities.
Other community development and amenities	4,202 (32%)	EPC	The driver of these expenses is state population.
		Wage costs	Recognises the differences in wage costs between states.
		Regional costs	Recognises the higher costs of providing services to remote communities.
Environmental protection	6,366 (49%)	Non-deliberative EPC (a)	These expenses are not differentially assessed.
		Wage costs	Recognises the differences in wage costs between states.
		Regional costs (b)	Recognises the higher costs of providing services to remote communities.

(a) Non-deliberative EPC means the Commission was unable to find a driver of need. The expenses cover a wide variety of services and it was considered neither practical to disaggregate these expenses nor possible to identify a single broad indicator for assessing total spending.

(b) Applied only to the protection of biodiversity and landscape sub-component (which includes national parks and wildlife).

Source: Commission calculation.

GST Distribution in the 2023 Update

14 The extent to which the assessment results in a different distribution of GST compared with an equal per capita distribution is shown in Table 4. It shows the category distributed $623 million ($24 per capita) away from an equal per capita share. Although most state spending relates to environmental protection and other community development, the components most influencing the GST distribution are First Nations community development and electricity and water subsidies in remote and small communities respectively.

Table 4 GST impact of the services to communities assessment, 2023–24

	NSW	Vic	Qld	WA	SA	Tas	ACT	NT	Total effect
	$m	$m	$m	$m	$m	$m	$m	$m	$m
Water subsidies	-20	-37	16	7	8	12	-5	20	62
Electricity subsidies	-146	-135	41	111	8	-3	-9	134	293
First Nations community development	-92	-98	25	27	-16	-8	-7	170	221
Other community development and amenities	2	-9	-4	10	-4	-1	2	4	18
Environmental protection	9	-8	-10	14	-7	-3	3	3	28
Total ($m)	**-248**	**-287**	**68**	**167**	**-11**	**-3**	**-17**	**330**	**623**
Total ($pc)	**-30**	**-42**	**12**	**59**	**-6**	**-5**	**-35**	**1,270**	**24**

Source: Commission calculation, 2023 Update.

15 Further detail on service provision arrangements, the scope of the adjusted budget and the underlying conceptual cases for the assessment methods are explained in Volume 2 Chapter 18 ‘Services to communities’ of the Report on GST Revenue Sharing Relativities, 2020 Review.

What has changed since the 2020 Review?

Potential increase in government spending on natural disaster mitigation

16 State spending on natural disaster mitigation is not separately assessed. These expenses are likely to be classified to either the environmental protection component in the services to communities category or to the other expenses category and assessed on an equal per capita basis.

17 The frequency and severity of natural disaster events is predicted to further increase.[3] The Commission is seeking state views on whether there will be a significant increase in spending on natural disaster mitigation in the near term in response to changes in the climate, which may justify a separate assessment of these expenses.

[3] Royal Commission into National Natural Disaster Arrangements, ‘Royal Commission into National Natural Disaster Arrangements Report,’ Canberra, 2020, Royal Commission into National Natural Disaster Arrangements Report (accessed 4 June 2023).

Implications for assessment

18 The Commission's preliminary view is that the services to communities assessment methods remain fit for purpose.

19 However, one issue has been identified for consideration during the 2025 Review:

- if states increase spending on natural disaster mitigation, should these expenses be assessed separately from other environmental protection expenses?

Potential increased spending on natural disaster mitigation

20 If greater recognition of the consequences of climate change results in increased spending on natural disaster mitigation, the Commission may need to consider separately assessing state needs for mitigation spending.

21 Consistent with the assessment guidelines, a separate assessment would require:

- a conceptual case that some states need to spend more than others on natural disaster mitigation (driver of need)
- a reliable method for estimating the driver of need
- data that are fit for purpose and of suitable quality
- a material impact on the distribution of GST.[4]

Existing state spending on natural disaster mitigation

22 For many years the National Partnership on Disaster Risk Reduction has supported state initiatives to mitigate the effects of natural disasters. The current agreement runs from March 2020 to June 2024. For each year of the agreement, total spending is estimated to be around $42 million, funded equally by the Commonwealth and the states (see Table 5). The Commission treats the Commonwealth payment as no impact on the basis that needs are not assessed for environmental protection.

[4] Following state consultation on the 2025 Methodology Review paper 'Fiscal equalisation, supporting principles and assessments guidelines', the Commission has increased its materiality threshold to $40 per capita (for the assessment of a driver) and $12 per capita (for a data adjustment).

Table 5 Estimated financial contribution, National Partnership on Disaster Risk Reduction

	2019-20	2020-21	2021-22	2022-23	2023-24	Total	Ratio to population share
	$m	$m	$m	$m	$m	$m	
Estimated total budget	41.8	41.8	41.8	41.8	41.8	208.8	
Estimated National Partnership Payments	20.9	20.9	20.9	20.9	20.9	104.4	
NSW	5.4	5.4	5.4	5.4	5.4	27.1	0.8
Victoria	3.3	3.3	3.3	3.3	3.3	16.7	0.6
Queensland	4.8	4.8	4.8	4.8	4.8	24.0	1.1
Western Australia	2.5	2.5	2.5	2.5	2.5	12.5	1.1
South Australia	1.7	1.7	1.7	1.7	1.7	8.4	1.1
Tasmania	1.0	1.0	1.0	1.0	1.0	5.2	2.3
ACT	1.0	1.0	1.0	1.0	1.0	5.2	2.8
Northern Territory	1.0	1.0	1.0	1.0	1.0	5.2	5.2

Source: National Partnership Agreement on Disaster Risk Reduction (federalfinancialrelations.gov.au)

23 The distribution of funding to the states under the National Partnership on Disaster Risk Reduction 'is based on population, cost of disasters and relative disadvantage, and is adjusted by agreement to provide an adequate minimum level to Tasmania and the Territories'.[5]

24 The Commission consulted the National Emergency Management Agency to seek further information on its method for distributing national partnership payments to the states. The National Emergency Management Agency noted that the existing formula has long been used in the natural disaster mitigation partnership agreements. The underlying data on the costs of natural disasters comes from the 2001 Bureau of Transport Economics report 'Economic Cost of Natural Disasters in Australia', which collated information on the cost of natural disasters from 1967 to 1999.[6]

25 More recently, the Commonwealth has established the Disaster Ready Fund to jointly fund mitigation projects with states. The Disaster Ready Fund commits up to $200 million per year.

26 Funding from the Disaster Ready Fund will support activities aligned to the National Disaster Risk Reduction Framework that:

- take action to reduce current disaster risk
- minimise creation of future disaster risk

[5] National Partnership on Disaster Risk Reduction, 2020, p. 7 see https://federalfinancialrelations.gov.au/sites/federalfinancialrelations.gov.au/files/2020-05/disaster_risk_reduction.pdf (accessed 8 June 2023)

[6] Bureau of Transport and Regional Economics, 'Economic Cost of Natural Disasters in Australia,' Canberra, 2001, Bureau of Transport and Regional Economics, Economic Cost of Natural Disasters in Australia (bitre.gov.au) (accessed 4 June 2023).

- equip decision-makers with the capabilities and information they need to reduce disaster risk.

27 Projects to be supported through the Disaster Ready Fund could include flood levees, floodways, seawalls, firebreaks, and constructed wetlands and reefs. Projects that target systemic risk reduction to improve the quality and impact of the response to future disasters will also be eligible.

28 In February 2023, the Commonwealth commissioned an independent review into Australia's disaster funding arrangements, to ensure government investment in disaster funding is fit-for-purpose and effective in the face of increasingly frequent and more severe natural disasters. The Review will consider how government investment in disaster risk reduction, preparedness, response, recovery and resilience can better support a national system. It will also look at what will be needed to build resilience to the extreme disaster events Australia is projected to experience over the coming decades. A final report is expected to be provided to the government in April 2024.

29 A common understanding of what constitutes natural disaster mitigation will be needed to ensure consistency in expense reporting. Ideally, the Commission would adopt a definition that is already being used by states, such as the definition in the National Partnership on Disaster Risk Reduction:

Disaster: *A serious disruption of the functioning of a community or a society at any scale due to hazardous events interacting with conditions of exposure, vulnerability and capacity, leading to one or more of the following: human, material, economic and environmental losses and impacts.*[7]

Disaster risk reduction: *Disaster risk reduction is aimed at preventing new and reducing existing disaster risk and managing residual risk, all of which contribute to strengthening resilience and therefore to the achievement of sustainable development.*[8]

Conceptual case for a driver of need for spending on natural disaster mitigation

30 The scale, severity, frequency and type of natural disasters vary across states.[9] The Royal Commission into National Natural Disaster Arrangements stated:

> 'Each state and territory varies in its experience of natural hazards. Each has its own climate, geography and environment that influence the type, frequency, intensity and severity of hazards experienced.

[7] National Partnership on Disaster Risk Reduction, 2020, p. 8 see https://federalfinancialrelations.gov.au/sites/federalfinancialrelations.gov.au/files/2020-05/disaster_risk_reduction.pdf (accessed 8 June 2023)

[8] National Partnership on Disaster Risk Reduction, 2020, p. 9 see https://federalfinancialrelations.gov.au/sites/federalfinancialrelations.gov.au/files/2020-05/disaster_risk_reduction.pdf (accessed 8 June 2023)

[9] Year-to-year variation is also high, which has implications for the appropriate time period used to assess state risk, if historical data is to be used.

> As a result, the resourcing and arrangements in mitigating and responding to natural hazards also varies in each jurisdiction.'[10]

31 The Commission has not come to a preliminary view on how to assess spending by states to mitigate the impact of natural disasters. There is currently insufficient information, particularly reliable and consistent data on state mitigation expenses, and a reliable driver of such spending.

32 Given the potential for a significant increase in state spending on natural disaster mitigation in the near term, the Commission will continue to monitor developments. If considered appropriate, a change to how this expenditure is assessed may need to be discussed with the states.

Consultation questions

Q1. Do states agree that the existing assessment methods for spending on disaster mitigation remain appropriate?

Q2. Do the definitions used in the National Partnership on Disaster Risk Reduction provide an appropriate basis for describing the type of spending that could be classified as natural disaster mitigation?

Q3. Where is this spending currently classified in the Government Finance Statistics framework?

Q4. Is spending on mitigation measures expected to increase significantly over the next five years?

Proposed assessment

Differences from the 2020 Review approach

33 Subject to state views, the Commission does not propose to make changes to its 2020 Review approach.

Proposed assessment structure

34 Table 6 shows the proposed structure of the services to communities assessment.

[10] The Royal Commission into National Disaster Arrangements, 'Royal Commission into Natural Disaster Arrangements Report, Canberra, 2020, see https://naturaldisaster.royalcommission.gov.au/publications/html-report/chapter-02 (accessed 8 June 2023)

Table 6 Proposed assessment structure for services to communities

Component	Driver	Influence measured by driver	Change since 2020 Review
Water subsidies			
Small communities	Small communities	Recognises that costs are higher for small communities.	
	Regional costs	Recognises the higher costs for small communities in outer regional and remote areas.	No
	Wage costs(a)	Recognises the differences in wage costs between states.	No
Other	EPC	The driver of these expenses is state population.	No
Electricity subsidies			
Remote communities	Remote communities	Recognises that costs are higher for remote communities.	No
	Regional costs	Recognises the higher costs for providing services in very remote communities.	No
	Wage costs(a)	Recognises the differences in wage costs between states.	No
Other	EPC	The driver of these expenses is state population.	No
First Nations community development	Population in discrete First Nations communities	Recognises the higher costs of providing services in discrete First Nations communities.	No
	Wage costs(a)	Recognises the differences in wage costs between states.	No
	Regional costs	Recognises the higher costs of providing services to remote communities.	No
Other community development and amenities	EPC	The driver of these expenses is state population.	No
	Wage costs(a)	Recognises the differences in wage costs between states.	No
	Regional costs	Recognises the higher costs of providing services to remote communities.	No
Environmental protection	Non-deliberative EPC	These expenses are not differentially assessed.	No
	Wage costs(a)	Recognises the differences in wage costs between states.	No
	Regional costs (b)	Recognises the higher costs of providing services to remote communities.	No

(a) The Commission will consult with states on the wages assessment in a separate paper.
(b) Applied only to the protection of biodiversity and landscape sub-component (which includes national parks and wildlife).
Source: Commission calculation, 2023 Update

New data requirements

35 Disaggregated state data on electricity and water services, expenses and revenue at the community level are updated at the start of the review and used for the duration of the review. Information on the timing of these data requests will be provided in July 2023.

Consultation

36 The Commission welcomes state views on the consultation questions identified in this paper (outlined below) and the proposed assessment. State views should accord with the 2025 Review framework. States are welcome to raise other relevant issues with the Commission.

Q1. Do states agree that the existing assessment methods for spending on disaster mitigation remain appropriate?

Q2. Do the definitions used in the National Partnership on Disaster Risk Reduction provide an appropriate basis for describing the type of spending that could be classified as natural disaster mitigation?

Q3. Where is this spending currently classified in the Government Finance Statistics framework?

Q4. Is spending on mitigation measures expected to increase significantly over the next five years?