

Commonwealth payments

Overview

- 1 On 27 June 2023, the Commission issued a [consultation paper](#) on the draft Commonwealth payments assessment. The paper considered changes since the 2020 Review and their implications for the assessment method.
- 2 The Commission proposed to retain the 2020 Review assessment method with 2 additional elements:
 - a default ‘impact’ treatment for payments where there is substantial uncertainty about whether relevant state expenditure needs are assessed or the purpose of the payment
 - excluding Commonwealth own-purpose expenses (COPEs) from the scope of payments considered.
- 3 A summary of state and territory (state) responses to each consultation question is included below, as well as the Commission’s draft position and the draft 2025 Review assessment method.
- 4 State submissions can be viewed [here](#).

Consultation questions

Q1. Do states agree the guideline for deciding the treatment of Commonwealth payments remains appropriate?

State views

- 5 All states said the guideline remains appropriate, although Queensland and the Northern Territory qualified their agreement.
- 6 Queensland said it agreed subject to a discount being applied to the National Health Reform Agreement payments to offset higher expenses incurred by states on hospital services due to perceived deficiencies in Commonwealth funding of primary and aged care services.
- 7 The Northern Territory said it broadly agreed subject to the guideline clarifying that payments aimed at addressing structural disadvantage belong to a category of services where the Commission does not assess need. The Northern Territory also said the framework should clarify that mixed-purpose agreements with separated funding schedules may attract different GST treatments.

Commission response

- 8 Queensland's suggestion for a discount to the National Health Reform Agreement is addressed in the health chapter of this report.
- 9 The Commission notes the Northern Territory's issue regarding payments aimed at addressing structural disadvantage. If payments for structural disadvantage are separately identified and needs are not assessed, the payment would be treated as no impact according to the guideline. This issue is discussed further in the section on payments for structural disadvantage below.

Commission draft position

- 10 The Commission considers its existing guideline for deciding the treatment of Commonwealth payments remains appropriate. It proposes to retain the guideline, with additional guidance on its implementation discussed below.

Q2. Do states agree to a default treatment of 'impact' in cases where there is substantial uncertainty about the payment's purpose or whether relative state expenditure needs are assessed? It remains open to states to provide evidence in support of no impact.

State views

- 11 Most states said they agreed with a default impact treatment for payments where there is substantial uncertainty about the purpose of a payment or uncertainty about whether the Commission is assessing needs. Some states said such an approach would give a degree of certainty on the treatment of new payments.
- 12 Queensland and Tasmania emphasised that states should continue to be afforded the opportunity to present a case, supported by evidence, where they disagree with the impact treatment. Queensland said the Commission should continue to assess payments on a case-by-case basis and should be willing to reconsider its decision in light of new evidence. Western Australia said if states are able to challenge the default treatment after the new issues paper is released, other states should also be given the opportunity to respond.
- 13 South Australia proposed an alternative approach. It said uncertain payments could be treated 50% impact and 50% no impact. It said this approach would moderate the redistribution compared to a default impact treatment.

Commission response

- 14 The Commission will continue to consider Commonwealth payments on a case-by-case basis. Where it is clear that a payment is not for a state service or that needs are not assessed, the payment will be treated as no impact. The default impact treatment is only intended to apply to the minority of payments where the

Commission is uncertain if they fund a state service or if they fund expenditure for which the Commission assesses needs.

- 15 In response to the issues raised by Queensland and Tasmania, the Commission notes that states will continue to have the opportunity to challenge the default impact treatment as part of the new issues process in an annual update of GST relativities. It also agrees that states should have the opportunity to respond to the comments of other states in cases where the Commission is considering changing its initial view.
- 16 The Commission recognises that the South Australian proposal to adopt a 50% impact treatment of uncertain payments is a simple approach to deal with payments where there is substantial uncertainty. However, the Commission considers the proposed approach of defaulting to an impact treatment, with states having the opportunity to challenge the outcome, is more consistent with equalisation than an arbitrary 50/50 split.

Commission draft position

- 17 The Commission proposes to adopt a default treatment of impact in the small number of cases where there is substantial uncertainty about whether a Commonwealth payment is for a state service for which needs are assessed. States will continue to have the opportunity to challenge this default treatment.

Q3. Do states agree to discontinue the assessment of Commonwealth own-purpose expense payments?

State views

- 18 Most states supported the proposal to discontinue the assessment of COPEs. Several states said that assessed COPEs make up a very small proportion of Commonwealth payments and there is not a comprehensive list of COPEs. Western Australia said the current approach of considering some COPEs but not others was inequitable. It added that if they were properly classified as COPEs by the Commonwealth, they should be treated as no impact. While Victoria and South Australia supported the proposal, they said if the quantum (or materiality) of COPEs increased in the future, their exclusion should be reviewed.
- 19 New South Wales said that conceptually all Commonwealth payments that support state services for which needs are assessed should be considered, including COPEs. It said the Commission should test the materiality of identified COPEs and only exclude those that do not meet a materiality threshold. New South Wales said the issue was similar to the treatment of state health services provided by the private sector. It said in both cases a state is relieved from the need to undertake expenditure and that this should be captured in the Commission's assessments.

Commission response

- 20 In keeping with the Commission's guideline for the treatment of Commonwealth payments, all payments that support states services, or that relieve a state from providing a service, should be included as impact.¹ However, in the absence of comprehensive data on COPEs, the Commission is only able to consider a limited number of COPEs paid to state entities – those which are easily identifiable or have been brought to the Commission's attention by states. In addition, the Commission does not have visibility of COPEs paid to non-government organisations, some of which may reduce the amount a state needs to spend on a service.
- 21 The Commission also notes there has been a significant reduction in the value of COPEs included in assessments since the transition to the current Federal Financial Relations framework in 2009. It is unclear whether the reduction reflects an overall reduction of COPEs by the Commonwealth, or a shift towards funding activities through non-government organisations rather than state governments. While the Commission does not apply a materiality threshold to Commonwealth payments, it observes that there is only one COPE (Rural and other health grants) that would be material at the \$40 per capita driver threshold and this is only material for the Northern Territory.
- 22 Under the New South Wales proposal, the Commission could continue to assess single material COPEs. However, given the possibility of unidentified COPEs paid to states, the Commission considers removing all COPEs from the assessment is a more consistent and equitable approach.
- 23 To test the materiality of individual COPEs on a case-by-case basis as proposed by New South Wales or monitor the quantum of COPEs as suggested by Victoria and South Australia, the Commission would have to continue requesting data from numerous Commonwealth Government agencies. On practicality grounds, the Commission is not inclined to do this. However, if there are significant changes to Federal Financial Relations, or evidence of significant increases in funding paid to states outside of the Federal Financial Relations framework, the Commission may review its position.

Commission draft position

- 24 Given the small size of identified COPEs and the difficulty in comprehensively identifying all COPEs, the Commission proposes to cease including the revenue paid to states in the form of COPEs in its Commonwealth payments assessment.²

¹ The Commission's guideline is outlined in the [consultation paper](#).

² The Commission notes that, to the extent COPEs are captured in ABS Government Finance Statistics data, they will be reflected in the Commission's 'balancing item'. The balancing item ensures the sum of individual Commonwealth payments sourced from the Commonwealth Final Budget Outcome matches total Commonwealth payments in Government Finance Statistics data. The balancing item does not move states' relative fiscal capacities away from an equal per capita assessment.

Q4. Do states agree that the guideline for determining the GST treatment of Commonwealth payments should be applied in cases where payments include elements aimed at addressing pre-existing structural disadvantage?

State views

- 25 Most states said the Commission's guideline remains valid in the cases where payments include elements that are aimed at addressing pre-existing structural disadvantage. Seven states said payments aimed at addressing structural disadvantage are best excluded through the terms of reference for an update.
- 26 New South Wales said if a state considers a payment to be outside average policy, it should be required to provide evidence that expenditure needs are not assessed. South Australia said there was a risk of overcompensation relative to actual state needs if a payment was excluded where expenditure needs are actually assessed.
- 27 New South Wales said equalisation by itself will not necessarily provide states with the sufficient funding to overcome disadvantage. It said that if it is average policy to address specific forms of disadvantage, then equalisation will act to distribute funds to states according to their differential needs.
- 28 New South Wales said to decide whether to treat Commonwealth funding related to overcoming disadvantage as no impact, the Commission would first need to determine the extent to which states' existing expenditure efforts are already reflected in an assessment. It said any payment that a state considers outside of average policy should require the state to provide evidence of how the corresponding expenditure is not captured in the expenditure assessments.
- 29 The Northern Territory said that payments aimed at addressing pre-existing structural disadvantage should be excluded from the GST calculations. It said payments aimed at addressing pre-existing structural disadvantage are driven by the aim of achieving outcomes that are not currently met, rather than the delivery of state average services and therefore should be excluded from the assessment for the purpose of fiscal equalisation.
- 30 The Northern Territory said fiscal equalisation seeks to equalise to the average level of services delivered by jurisdictions. This can lead to significant divergence in outcomes as average expenditure level makes no allowance for whether the expenditure is sufficient to achieve similar outcomes for all persons or within all jurisdictions. It said excluding payments aimed at addressing pre-existing structural disadvantage is a clarification of the existing guidelines for excluding payments for services which needs are not assessed.

Commission response

- 31 The Commission considers that there is scope within the existing guideline to consider whether payments relating to structural disadvantage should be excluded from the GST calculations. If needs for structural disadvantage are not assessed, then payments for such purposes should be excluded from impacting the GST distribution as per the current guideline.
- 32 The Commission agrees with the view of 7 states that for clarity it would be preferable for the terms of reference for an update to exclude payments for structural disadvantage. Should the terms of reference not quarantine these payments, this will not necessarily preclude the Commission from making a no impact decision if it concludes that the payment is for existing structural disadvantage and the needs are not assessed. The Commission agrees with New South Wales that any such decision should be based on evidence provided to the Commission.

Commission draft position

- 33 The Commission considers that it should apply its existing guideline for deciding the treatment of payments to all Commonwealth payments, including those that might contain elements addressing pre-existing structural disadvantage.
- 34 In taking this position, the Commission notes that if there is clear evidence that a payment or part payment is for pre-existing structural disadvantage and needs are not assessed, it will be treated as no impact.

Other issues raised by states

Commonwealth-state disagreements about the nature of a payment

- 35 New South Wales said it had concerns about cases where the Commonwealth Treasury and a state disagree on the nature of a specific payment. It said, in such cases, the Commission should come to a decision on the matter through its own analysis, rather than solely relying on the Commonwealth Treasury's position.
- 36 New South Wales cited the specific example, from the 2020 Review, of a payment under the Skilling Australia Fund that New South Wales considered a reward payment, but the Commonwealth Treasury did not. New South Wales said where the Commission relies solely on Commonwealth Treasury advice, there may be a disincentive for states to enter a funding agreement, if the benefit to the state is reduced by the GST redistribution.
- 37 New South Wales said although this issue would ideally be managed between the Commonwealth and the states, there was a role for the Commission in the event of

a dispute. It said there would be benefit in the Commission reconciling the reward payments identified by the Commonwealth with those identified by each state.

Commission response

38 Terms of reference specify a default no impact treatment for reward payments. In response to the comments from New South Wales, the Commission contacted Commonwealth Treasury and it confirmed previous advice that there were no reward payments in recent updates. The Commission may not always be well placed to determine whether a payment meets the definition of a reward payment. The Commission will continue to be guided on these issues with advice from the Commonwealth Treasury and the states, as well as considering published national agreements.

Commission draft position

39 The Commission proposes to continue to apply its existing guideline for deciding the treatment of Commonwealth payments. Where appropriate, it will continue to be guided by the advice of Commonwealth Treasury and the states, as well as considering published national agreements, to determine which payments are reward payments.

Draft 2025 Review assessment method

- 40 Following consideration of state views, the Commission proposes to retain the 2020 Review assessment method with 2 changes to its implementation:
- a default impact treatment will be adopted for payments where there is substantial uncertainty as to whether or not a Commonwealth payment is for a state service for which needs are assessed
 - COPEs will no longer be included in the assessment.
- 41 Table 1 shows the proposed structure of the 2025 Review Commonwealth payments assessment.

Table 1 Proposed structure of the Commonwealth payments assessment

Component	Driver	Influence measured by driver	Change since 2020 Review?
Impact payments	Actual payments per capita	Recognises that states which receive above-average per capita Commonwealth payments have greater fiscal capacity.	No

Indicative distribution impacts

- 42 The impact on the GST distribution in 2024-25 from the proposed changes is shown in Table 2. Removing COPEs from the assessment would increase the GST distributed to the Northern Territory and reduce the distribution to New South Wales, Victoria, Queensland and Tasmania.

Table 2 Indicative revenue impact on GST distribution (difference from an equal per capita distribution), 2024–25

	NSW	Vic	Qld	WA	SA	Tas	ACT	NT	Total Effect
	\$m	\$m	\$m	\$m	\$m	\$m	\$m	\$m	\$m
U2024 using R2020 methods	685	1,400	-1,310	-344	52	-116	154	-521	2,291
U2024 using draft R2025 methods	663	1,375	-1,320	-344	54	-117	156	-466	2,248
Effect of draft method changes	-22	-25	-10	0	3	-1	1	54	-59
	\$pc	\$pc	\$pc	\$pc	\$pc	\$pc	\$pc	\$pc	\$pc
U2024 using R2020 methods	80	199	-234	-116	27	-200	322	-2,028	84
U2024 using draft R2025 methods	78	195	-236	-116	29	-202	325	-1,816	82
Effect of draft method changes	-3	-4	-2	0	1	-1	3	212	-2

Note: The GST pool and population estimates are equivalent to those used in the 2024 Update.

The data included in the table have not been subject to full quality assurance processes and as such, should be treated as indicative only.

Indicative GST impacts are provided for illustrative purposes only and should not be used to predict impacts on GST distribution for 2025-26.

- 43 The Commission proposes to change the treatment of the Commonwealth payments *COVID-19 public health response* and *Support for businesses impacted by COVID-19* lockdowns from a no-impact treatment to an impact treatment. The impact of this change is not included in Table 2. More information on those changes is provided in the health and services to industry chapters.