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### **Inquiry in the GST Distribution Reforms**

Dear GST Review Committee,

I am pleased to make this submission to the Inquiry in my capacity as Director of the Australian Centre for Federalism. This submission reflects the work and expertise of the Centre and has been prepared in collaboration with Dr. Thiago N. da Silva, Deputy Director of the Centre.

I am an academic specialist in comparative federalism and intergovernmental relations at the Australian National University (ANU), where I am a full-time faculty member in the School of Politics and International Relations (SPIR). In addition to my academic roles, I have served as a consultant and adviser on federalism and the design of federalised policy arrangements for organisations including the World Bank, UNICEF, national governments, and non-government organisations.

Since 2023, my research has focused on Australian fiscal federalism and Commonwealth–State financial relations. I have authored six peer-reviewed publications and two forthcoming chapters in leading journals and academic presses on issues including subnational public debt in Australia, the 2018 reforms to horizontal fiscal equalisation from full to partial equalisation (with Professor Miranda Stewart)<sup>1</sup>, and the implications of *Vanderstock v. Victoria* for Commonwealth–State fiscal relations. In 2024, I presented this last work to the Chief Justice and Justices of the High Court of Australia, Justices of State Supreme Courts, and the Solicitor-General of Australia.

In my most recent research (with Dr. Silva)<sup>2</sup>, we use Australia as a case study to examine how citizens assess whether they are treated fiscally fair by the Commonwealth—based on the state/territory where they reside. This research demonstrates that, beyond individual income, place-based context—including whether citizens reside in socio-economically advantaged or disadvantaged areas—plays a significant role in shaping attitudes towards intergovernmental fiscal redistribution.

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<sup>1</sup> Fenwick, T.B. and M. Stewart. (2025). [Chapter 4 From Full to Partial Equalisation: The Case of Horizontal Fiscal Equalisation in Australia](#) in Erkoreka, Mikel, Kolling, Mario (eds.), *Fiscal Equalisation, Intergovernmental Transfers and Territorial Inequalities in Federations*, Brill Press, Leidan.

<sup>2</sup> Fenwick, T. B., & Silva, T. N. (2026). Income, place and perceptions of fiscal fairness: evidence from Australian federalism. *Territory, Politics, Governance*, 1–17.  
<https://doi.org/10.1080/21622671.2026.2615939>

This submission draws on original public opinion data from this project and into my wider research into the politics of territorial (re)distribution. I focus herein on implications of the 2018 HFE reforms, including public opinion and legitimacy from our collaborative research, the pros/cons of possible reform scenarios circulating in this policy space, and finally, I make a final recommendation and suggest broader issues for the commission to consider.

**The Problem: Why the 2018 legislative changes politicised the distribution of the GST and cannot be easily fixed post-facto (Information Request 1 & 2)**

Academic specialists in fiscal federalism and practitioners around the world have long regarded Australia's HFE as an example of best practice. The key features of the **pre-2018 HFE** that have underpinned this reputation are:

- an independent, arm's-length agency (**CGC**)
- joint accounting for State/Territory **expenditure needs** and revenue-raising capacity
- the inclusion of other **Commonwealth payments** to the states by the CGC, thereby equalising away, over time, the effects of special payments to certain states that might otherwise be considered politically motivated (pork-barrelling)
- its ability to generate **low levels of intergovernmental political conflict**.

It is this last feature of the pre-2018 HFE system that is most important to understand before any future reforms are proposed. First, before the creation of a guaranteed minimum relativity floor (currently **0.75**), Australia's HFE was largely insulated from states/territories targeting the Commonwealth with claims of unfairness. This type of vertical intergovernmental conflict occurs in other, more vertically designed equalisation systems, such as Canada's. Although the GST in Australia was enacted as a Commonwealth tax, it has been hypothecated as a states' tax.

*Pre-2018*, under full equalisation, the amount of GST to be distributed among the states was fixed, leading to the zero-sum nature of the distribution. This simply refers to the fact that if some states received more than their per-capita share of GST according to the CGC's calculations, others states received less, in order to balance the total share distributed among the states/territories.

**All of this changed, however, after the 2018 reforms**, which *de facto* created a dynamic whereby the Commonwealth is now the target of HFE tensions, rather than as previously these tensions occurring between the states themselves. Why?

First, the reforms to the HFE were perceived by the Australian public and state leaders as a response to political pressures from Western Australia. The decision was made exclusively by the Australian Government in 2018, upsetting the perceived **political neutrality** of the HFE. Even though the CGC is an independent, arm's-length agency, it follows Terms of Reference (ToRs) that are at the discretion of the Prime Minister and Treasurer of the Commonwealth.

Second, the **GST pool top-ups**—a payment made in perpetuity external to the GST—increased the size of the pool to be allocated among the states. The GST pool top-ups were *not* intended

to alter the zero-sum nature of the HFE system. The transitional **No-Worse-Off** (NoWo) payments, however—not intended to be permanent—*did* change the rules of the HFE game. This is because:

1. the payments were intended to ensure that the 2018 reforms did not make any state or territory worse off, thereby decreasing the potential for increasing horizontal tensions and interstate conflict
2. the NoWo payments made all states/territories winners of the 2018 reforms (not just WA) because they injected an additional **\$14.6 billion** into the HFE, which benefited all jurisdictions
3. the extension by the Albanese Government of the NoWo payments, and their continued funding from outside the GST pool, signals de facto a shift away from a strictly zero-sum HFE system towards a positive-sum model financed by Commonwealth top-ups. This means that, should the Commonwealth cease providing the NoWo payments, it would become the clear political target of the states/territories, as total funds available to all jurisdictions would fall.

There is **no easy policy fix to the 2018 reforms**. If the NoWo payments cease, the minimum GST revenue-sharing relativity would also have to be removed; otherwise only one state (WA) would remain a winner—receiving more than its assessed relativity—while all other states and territories would receive less (i.e., they would de facto be made worse off relative to WA). Because subnational revenue-raising capacity is already extremely limited in Australia by fiscal constitutionalism, any decrease in the size of the revenue pool to be allocated via HFE would further reduce the ability of the states/territories to manage their finances. It would also provide state/territory leaders with a renewed opportunity to blame the Commonwealth for budget deficits and/or increase citizens' perceptions of unfair fiscal treatment.

According to our research (Fenwick & Silva, 2026), residents in four of the eight constituent units—**Tasmania, South Australia, Western Australia, and the Northern Territory**—in 2023 believed the state/territory in which they reside receives *less than its fair share* of federal funding.<sup>3</sup> This pattern indicates that residents in smaller, less populous, or more geographically remote jurisdictions are more likely to feel that their state or territory is disadvantaged in federal fiscal allocations—even though, in reality, these are the same jurisdictions that, on average in recent years, receive more than their per-capita share of GST because of higher assessed revenue and expenditure needs and/or the operation of the minimum relativity floor. Of particular interest, **NSW, Victoria, and Queensland**—the states whose relativities are closest to 1.0 (i.e., per-capita share)—are most likely to perceive the share of funding under the current arrangements, in those states, as “fair” (Fenwick & Silva, 2026).

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<sup>3</sup> See Biddle, Nicholas, 2023, "ANU Poll 56 (August 2023): Experiences with COVID-19, mental health and wellbeing, employment, fertility, and federalism", <https://doi.org/10.26193/AAZ3QI>, ADA Dataverse, V2 for raw results of survey data.

## Exploring Potential Reform Options: Increasing the Rate and Base of the GST vs. Reverting to the pre-2018 System (Information Request 4 &5)

Therefore, what potential **policy reform options** exist for the HFE? I strongly urge the GST Inquiry *not* to consider increases to the rate or base of the GST, as is often suggested by some economists because the GST is technically considered an efficient tax. **Why?** Many scholars and commentators fail to recognise a simple policy paradox that creates significant challenges for GST reform. Changes to the distribution of the GST *do not* require the approval of the states and territories—however, changes to the rate or base of the GST *do* require their collective consent. Therefore, if the states were to agree to raise the base and rate of the GST, who would distribute it and how? What legal guarantee would the constituent units have that an increased GST pool would benefit them? Under what conditions would they agree? These are not simple questions.

A larger and broader GST provides full discretion to any Commonwealth Government to alter the distribution of the GST as it chooses, opening the door to further Commonwealth–State fiscal arrangements being driven by political incentives, rather than by the goals of increasing the **fiscal flexibility** of the states/territories to respond to **economic volatility**, enabling them to balance their budgets, or decreasing the vertical fiscal imbalance (VFI) to make states and territories more accountable for their **fiscal management**.

In a second survey module we included in Biddle (2025)<sup>4</sup>, **our results** indicate that a majority of Australians in every state and territory—except the Northern Territory—support the current arrangements of the HFE. We then asked respondents about their preferences for GST allocation, specifically:

“Each State/Territory currently receives a minimum of 75 cents per GST dollar generated in that State/Territory regardless of that state/territory’s revenue capacity. This means that some States/Territories receive more money than their revenue and spending assessment.

Which of the following best represents your view on GST allocation?

1. Transfer GST funds on an equal per person basis to each state. This would transfer more GST money to the richer States/Territories.
2. Transfer based on revenue and spending assessments with no guaranteed amount of revenue per person. This would transfer more money to the poorer States/Territories.
3. Keep GST distribution as it is now.
4. Not sure.
5. Prefer not to say.”

The results show that **32.5 per cent** of respondents prefer to keep the current system (with a minimum revenue guarantee), **32.2 per cent** prefer to revert to the *pre*-2018 system, and only **17.4 per cent** support distributing the GST on an equal per-capita basis (an additional reform

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<sup>4</sup> See ANUpoll/ORU Federal Election Tracker, Wave 4 (May 2025) dataset. [DOI forthcoming: <https://dataverse.ada.edu.au/dataverse.xhtml?alias=anupoll>]

option circulating in the policy domain)—the rest didn't know/didn't answer. We then asked respondents whether they believe **Western Australia receives more benefits than it deserves**. Only 30 per cent strongly agreed or agreed; the remaining 70 per cent neither agreed nor disagreed, disagreed, or did not answer. This indicates that **seven out of ten Australians** have *no opinion or insufficient knowledge* about the GST's distribution to assess whether WA receives "more HFE than they deserve."

Beyond public opinion, put succinctly, for the Commonwealth, reverting to the *pre*-2018 HFE system is **not politically feasible**, as it would make all other states worse off and significantly increase tensions with Western Australia, thereby heightening intergovernmental conflict. For the states and territories, any HFE reform that reduces their fiscal allocations is **not economically feasible**, given the current levels of subnational public debt and rising budget deficits. While a larger and broader GST may be the Commonwealth's economic answer, it is highly unlikely to be politically accepted by the states without explicit guarantees over how it would be distributed—guarantees that would need to make all jurisdictions winners. Removing expenditure factors would be fundamentally unfair to all states given the structural heterogeneity inherent to Australia. Such a reform would signal the end of reasonable equalisation and the end of Australia's HFE as an example of global best practice. Therefore, what alternative options remain to achieve the outcomes expressed in the scope of the Productivity & Commission inquiry?

#### **Current & Alternative Arrangements (Information Request 4 &5)**

In my opinion, based on our research and the expertise cited above, the current arrangements deliver a reasonable level of HFE, and these arrangements are **generally supported** according to our research by public opinion. The current system also reduces economic volatility for Western Australia—and potentially for other resource-rich states such as Queensland—whose relativities may eventually fall below the minimum revenue threshold because of natural resources demand.

However, the current arrangements are not **fiscally efficient** from a federal perspective. The discrepancy between WA's assessed relativity for 2025–26 (0.18) and the revenue floor (0.75) (CGC, March 2025) has led to NoWo payments to the other states/territories far higher than those originally modelled by the Australian Government in 2018. The Canadian approach to resource revenues—only partially including a province's natural resource revenues in its revenue capacity calculations (roughly 50 per cent)—would have provided WA with a more stable GST share but one more reflective of its actual fiscal capacity, and at significantly lower cost to the Commonwealth than the current minimum relativity floor.

As noted in the Issues Paper, the additional **\$22.7 billion** already paid to the states, together with projected future payments, signals rising state/territory fiscal dependency on Commonwealth transfers, further widening Australia's already large—by international standards—vertical fiscal accountability gap.

The only **viable alternative** to support the states and territories to pursue reforms—including improving the efficiency of service delivery and strengthening state and territory revenue

bases—is to **reform Australia’s tax system** more broadly. The policy goals identified in the scope of this inquiry cannot be achieved through HFE or the GST alone. Neither the HFE nor the CGC—the agency responsible for calculating complex allocation formulas—was designed to allocate such large amounts of centralised revenues to the states and territories. The HFE was never intended to be such a significant revenue source for state and territory governments.

Increasing the size of the revenue pool to be allocated within the HFE—as has occurred since 2018 through pool top-ups, transition payments, and NoWo payments—further **obscures**, for both the public and the media, how the HFE operates, why, and whether it is “fair.” It also creates opportunities for state-level political leaders to use the HFE as a mechanism to target the Commonwealth for additional resources.

The Productivity Commission must recognise that the post-2018 reforms shifted the HFE from **a zero-sum logic to a positive-sum logic**, where greater resources external to the GST can be demanded from the Commonwealth—and have been provided. The implications of this shift are **politically irreversible**, and, given the extent of VFI in Australian fiscal federalism, are **fiscally unsustainable** for the Commonwealth.

An alternative arrangement is not just to increase the GST, but rather to share a **portion of the income tax** with the states and territories from where it was originally derived (for example, 50 per cent). This is more technically feasible for income tax because it is extremely difficult to identify the state of origin for GST collections. A sharing of income tax would provide room for the Commonwealth to increase the rate and base of the GST while allocating only a **portion of the GST** (for example, 50 per cent) to be equalised within the HFE.

Such a reform would reduce the VFI in Australia by ensuring that the share of income tax collected by the Commonwealth and returned to the states would become a hypothecated states’ tax, like the GST. The fiscal capacity of the larger, more populous states would naturally increase through their share of the income tax they actually generate, leaving a larger portion of the GST pool available for distribution to the smaller, less populous, or more geographically remote jurisdictions—those same jurisdictions whose residents, according to our research, perceive themselves as currently disadvantaged in federal fiscal allocations.

This **mixed-tax arrangement** would generate greater **fiscal accountability** and **efficiency** at the state/territory level and provide incentives for states and territories to promote reforms and policy innovation and improve service delivery. Their dependence on the GST as a major revenue source would decline as they gain an independently generated revenue stream, supplemented by a share of GST equalised through the HFE. The guaranteed revenue floor could be retained but applied to a smaller portion of the total GST pool, making the system more economically sustainable while still protecting the most disadvantaged jurisdictions.

How we *choose* to distribute the GST—and whether we incorporate additional funds external to the GST into the HFE—will continue to shape **Commonwealth–State fiscal relations** in profound ways. The 2018 reforms politicised the HFE, and there is no path back to earlier arrangements. We must instead look forward to new policy solutions that strengthen both the

**transparency** of Commonwealth transfers and the **accountability** of state and territory fiscal management. Simply increasing the size of the fiscal pie to be divided at the discretion of the Commonwealth will do neither. Nor should we expect the CGC to allocate an ever-growing share of state and territory revenue through increasingly complex and opaque methods that lie beyond the understanding of most citizens, many bureaucrats, most journalists, and even numerous scholars of taxation and intergovernmental transfers.

Yours Sincerely,

Associate Professor Tracy B. Fenwick