



**Australian Government**  
**Productivity Commission**

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**PRODUCTIVITY COMMISSION**

**INQUIRY INTO HORIZONTAL FISCAL EQUALISATION**

**MR J COPPEL, Commissioner**  
**MS K CHESTER, Commissioner**

**TRANSCRIPT OF PROCEEDINGS**

**AT CHURCHILL ROOM, SALAMANCA INN, 10 GLADSTONE  
STREET, HOBART, TASMANIA  
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5       **MS CHESTER:** Good morning, everyone. We'll get underway. We've  
got our first participants here, so we'll have a little five-minute efficiency  
dividend. Good morning and welcome to the seventh day of our public  
hearings for the Productivity Commission's Inquiry into Horizontal Fiscal  
Equalisation. I'm Karen Chester, the deputy chair of the Commission and  
10 one of the Commissioners on this inquiry. I'm joined by my fellow  
Commissioner, Jonathan Coppel.

I'd just like to begin and open our hearings by acknowledging the  
traditional custodians of the land on which we meet today, the  
Mouheneenner people. I'd like to pay my respects to elders past and  
15 present.

Now, this is the final day of public hearings for this inquiry. In the past  
couple of weeks, Jonathan, I and the team have cantered around Australia  
to Perth, Melbourne, Adelaide and Darwin, and we saved Hobart as lucky  
20 last. During that process we've heard from some 50 participants over seven  
days. This actually follows, as many of you would be aware, much  
consultation that we've already had today. We've had meetings with many  
participants, we've travelled to every State and Territory jurisdiction before  
our draft report meeting with State and Territory officials, academics and  
25 other interested parties. We've just cracked the centenary of submissions.  
So we've had 44 post-draft report submissions, which takes us to a nice 100.

Now, after these hearings we'll be working towards completing a final  
report which will be submitted to the Australian Government next year.  
30 Participants in those – that have been registered for hearings will be advised  
when the final report is released. Once we give a report to Government,  
under our Act they have 25 Parliamentary sitting days after completion to  
table it.

35       The purpose of today's hearings and all of our hearings is really just to  
facilitate public scrutiny of our work, get feedback on the draft report, what  
we got right, what we got wrong and what we missed altogether. We like  
to conduct the hearings in a reasonably informal manner, but because we  
have a transcript being recorded we can't take or entertain comments from  
40 the floor. But at the end of today's proceedings if there's somebody here  
who has not registered and has a burning desire to be heard on these issues,  
if we've got time, we'll allow you to make some brief comments.

Now, participants are invited to make short opening remarks and we  
45 like to keep those up to five minutes. That's really just so we've got enough

time to discuss matters that you've raised with us and that we'd like to get a better understanding of. Participants aren't required to take an oath; we just ask that you be truthful. You are welcome and, indeed, we like it when people do comment on the submissions and evidence we've received from other participants, especially from those in Western Australia, we found that we've had some feedback on.

The transcript will be available from the Commission's website following the hearings. Participant submissions to the inquiry, as everyone should be aware, are also available on the website. For any media representatives that are attending today – and I don't think we have any, which is – one. I hope you've been given the rules of play and engagement and you'll follow those religiously. Most importantly note though that we will not have any video or audio recording as soon as I finish these opening remarks. But given there's no camera crews, we've all avoided that one.

Now, there is some piece of legislation that means I'm meant to say the following words. In the unlikely event of an emergency that requires the evacuation of this building, I'm just going to say follow common sense and don't take the lifts. With no further ado, I'd like to invite our first participants to join us from the Tasmanian Council of Social Services.

If you just take your time, make yourself comfortable, grab a glass of water. Then when you are comfortable, if you'd just like to each state your name and the organisation that you represent just for the purposes of voice recognition for the transcript. Then if you'd like to make some brief opening remarks.

**MS GOODES:** Kym Goodes, CEO of the Tasmanian Council of Social Service.

**MR DALLA-FONTANA:** I'm Isaac Dalla-Fontana, I'm a graduate policy officer for Tasmanian Council of Social Service.

**MS GOODES:** We've prepared some slides, I think, to, I guess, value-add to the written submission that has come through. Just for context, the Tasmanian Council of Social Service is the peak body for the community services sector in Tasmania. We also represent low-income, disadvantaged Tasmanians; so we wear both hats. Our expertise that we bring today is not necessarily in the detail of tax transfer systems or even the Grants Commission, but rather, the human side of what happens when taxes are sent through to states and how our service system in Tasmania needs to be able to respond to the needs of our population; in particular, as a state with the most disadvantaged population in the country, what we would like to talk through, I guess, in terms of that impact.

- As you will see in the first slide, Tasmania is, sadly, a place of quite entrenched disadvantage. It's also the consistent beneficiary of the Commonwealth-to-state and state-to-state fiscal transfers. This is not the question. What we need to ask is whether the people of Tasmania can receive the standard of services expected and owed to all Australian citizens without the extent of these transfers. So the strong view of TasCOSS is that no, Tasmania's population experiences a degree of disadvantage across many decades and across economic cycles that needs the system as it is to stay in place.
- As indicated by the first graph, the economic fortunes of Australia's states and territories have diverged further over the past three decades. So through this time Tasmania's status as Australia's poorest and most disadvantaged state has remained unchanged. Slide 2 shows that our labour market has historically and consistently been soft compared to the other states and unemployment generally the highest in the federation.
- Slide 3 shows that in recent times our unemployment rate has fallen relative to other states. Our under-utilisation rate remains high. In fact, under-employment is now probably Tasmania's biggest challenge, a problem potentially greater than unemployment itself. There is simply more people looking for more hours of work than there are jobs. It also appears that, as supported by slide 4, this trend of economic returns increasingly going to large cities might be affecting Tasmania. There's not much that we can do about that as a state. Hobart as our capital city has a population of 220,000 people.
- Slide 5 shows us that part of the reason for our persistent disadvantage is our consistently low educational outcomes. Tasmania has the lowest attainment of Year 12 certificate rate of any other Australian state or territory besides the Northern Territory. This is also true across the population as a whole. Tasmania is the least likely to have finished year 12, according to the most recent Census data.
- Slides 6 and 7 show a small ray of hope, I guess, for want of a better way of putting it, a bit of a bright spot in the figures. That is, that our numbers of graduation at tertiary level are stronger in relative terms in recent years. However, the level of attainment in the younger population remains stagnated. That's a real concern to us, I guess, in terms of our future demographic profile, which we'll talk a little bit about.
- In slide 8 we can see that it seems that many of our young people with tertiary qualifications are heading elsewhere for work. Slides 8 and 9 are probably the most, I guess, startling slides in terms of our migration of young people what we would call off-island, versus the intake of older

5 Australians into Tasmania. So what we can see from that demographic migration data is that we lose our young people between the ages of 15 and 29. While some trickle back, in the main that part of our population leaves our island due to lack of employment opportunities and, in the main, they don't come back.

10 We would say that other states in Australia clearly benefit from the flow-out of our young population and in return for its young people, Tasmania has long received interstate migration of arrivals of people past or at retirement age. This has a huge burden on our system all on its own. So in the middle of the last century Tasmania's population was the youngest Australian territory in the country and we are now the oldest. That has a substantial impact on the services that we need to provide.

15 The effects of these flows mean that there is a large bite in our age profiling in the 20 to 39 age range right at the point where most states in Australia have a population bulge. This bite will accelerate Tasmania's impending population decline because it's the cohort that starts families and raises children. Tasmania's poor demographic will increase the demand for  
20 government services relative to other states and sharply reduce our ability by the state government to fund these services through its own revenue such as payroll tax and, perhaps more importantly, through taxes that are fuelled by population growth such as land taxes and stamp duties.

25 So even today the need for services are not being met by our current Tasmanian population and, sadly, our population suffers as a result of that. Tasmanians are more likely to die prematurely and they are more likely to die of avoidable causes than [people in] any other state or territory besides the Northern Territory, even when we take into account our age profile. The  
30 Tasmanian Government has limited policy levers to prevent the outflow of our young people and as large cities are increasingly magnets for people and capital, this trend will likely continue.

35 The Tasmanian Government and the Tasmanian people are especially vulnerable to changes in the equalisation process. Forty-one per cent of Tasmania's total budget revenue comes from GST payments, the most of any state, other than the Northern Territory. So this is more than five times the proportion of WA and approaching double for New South Wales and Victoria amounts.

40 TasCOSS believes – and it is obvious – that every one of the trends that we have discussed so far would be more severe if the Tasmanian Government lost a substantial proportion of its HFE payments and could no longer provide a standard of service equivalent to other Australian states  
45 and support the many jobs in Tasmania that are now created and in time

exist as part of that service system, both in health, education and across the community services sector.

5 The 2012 GST distribution review specifically recommended against  
incremental changes to the HFE, finding that half-measures were untenable  
and the only alternative way was the wholesale rewriting of Australia's  
intergovernmental relations. TasCOSS believes that nothing has changed  
10 enough in the respective capacities and needs of this state to come to any  
other conclusion other than that of the previous review. In Tasmania's  
unique context as Australia's smallest and poorest state or territory, the  
human cost of movement away from the full HFE would be devastating.  
Beyond its immediate human cost, it would hasten the vicious cycles of our  
15 demographic decline as it would spur faster emigration of our skilled young  
people, drain our working-age population and make it increasingly  
unfeasible for the state to fund services for the population that remained.

Given that we live in communities, not economies, we urge the  
Commission to give full consideration to the human cost of any reduction  
20 in the degree of a HFE.

**MS CHESTER:** Thank you very much, Kym, for those opening remarks.  
We might just kick off with – I guess, as you said in your opening remarks,  
you are bringing the human side to this equation. Indeed, the way HFE  
works is to try to equalise the fiscal capacity of the state. So when we look  
25 at the overriding principle being one of equity, there's kind of then – equity,  
for me, is about the individual, the human side and what flows through to  
them, whereas the way HFE does it is about giving a state or a territory  
government an equalisation of fiscal capacity. You kind of then look  
through to well, what actually trickles through to the individuals.

30 I'm not sure to what extent, and I didn't anticipate – we didn't expect  
you to be across the detail of how it works. Indeed, we sort of think that  
there's only probably 30 people in Australia that know how it works. Some  
of them reside in Tasmania. But when you actually look through to the  
35 expenses side of HFE – so what the CGC does is they assess the expenses  
by saying, "This is what Tasmania would need," and then they adjust those  
expenses for disabilities; so remoteness factors, Indigeneity, all those sorts  
of things. When you look at what's assessed for Tasmania and then what  
the Tasmanian Government actually spends the GST moneys on, there is a  
40 bit of a mismatch. Are you aware of that?

**MS GOODES:** Yes and no. There's certainly a desire from TasCOSS and  
in all of our advocacy work with our state government to see greater levels  
of transparency, I guess, in terms of where that money that's flowing into  
45 our state, through the Grants Commission, is directly attributed to what we

would consider to be appropriate policy and service outcomes. So while we're, as a small organisation, not able to draw it down to a potential level of detail, we certainly – in our State Budget advocacy work, our submissions to the state, are keen to see a greater level of transparency and a deeper understanding of where that income into our state is directly impacting, what we know from our (indistinct) data, from our demographic profile of need, how we – ensuring that that money is being spent in the way that it is intended to be spent.

10 **MS CHESTER:** That's why I raise it with you, because listening to your opening remarks and reading your post-draft report submission, you are very much looking at how that equalisation process works through to the equity, which is the individual. When you kind of then look at the numbers CGC does prepare for us, over the last six years, Tasmania actually against its assessed expenses is 7 percentage points under. That's fine and understandable. Some states are above and some are below because it's untied moneys. They can spend it on what they like.

20 But then when you look through to the categories where they are underspending around sort of welfare and services to communities – so services to communities is only 34.8 per cent of what they should be – what they're assessed as needing to spend for that fiscal capacity. Welfare is 87 per cent, housing 82 per cent, post-secondary education 83 per cent. So you can see that there's – when you talk about it from an equity perspective, it's kind of useful to then look through to see well, these are the assessed expenses, but what's the actual outcome and what other priorities have crowded out those assessed needs?

30 **MS GOODES:** That's right. We would say – and it's relevant, as it is almost daily in terms of media coverage but also the focus through parliamentary processes, inquiries, our hospital system is a major challenge for us as a state. In terms of the government's allocation across its budget, we would be arguing strongly that we won't, in fact, stem the tide in terms of the chronic – proportion of chronic illness in our population, for example, which means that our hospital system is disproportionate in its funding needs to areas like housing, welfare. We have limited investment, we would argue, in preventative health measures.

40 So in terms of turning the tide around and looking at how in 50 years' time we could be having a different conversation, we would absolutely agree that there needs to be a greater accountability and a greater transparency around where both previous and current state governments are putting their focus in terms of those funds. Where it is in untied grants, we would argue strongly that if we cannot address our educational outcomes as a priority in this state we will continue to stay in the state of disadvantage that we're in.



I know Saul Eslake is presenting later on this morning. Saul, I'm sure, will talk about the fact that we spend more on education in Tasmania for students per head of population than any other state or territory and we still get the worst outcomes. TasCOSS argues strongly and consistently that we need to look at different ways of working if we are to get different outcomes for our population. I think what you're highlighting in terms of some discrepancies, I guess in funds in – versus expenditure, we would argue is one of the first places we need to go with that.

**MS CHESTER:** That's only even then – not even looking at the effectiveness of that system, which is, I think, what you're coming to and what Saul will focus on. Indeed, our recent five-year productivity review had a whole section of it dedicated to better educational outcomes, particularly for our young Australians. Indeed, some of the areas we went into there, we were informed by earlier discussions we had with senior officials at Tasmanian Department of Premier and Cabinet early on, very much around that mismatch that you've got between educational outcomes and economic participation.

**MS GOODES:** That's right. I guess the other Productivity Commission report that we are strongly focused on at the moment is around regional Australia and regional economies. We will be putting a strong case to the government and both major parties, basically, leading into the election that in terms of the GST revenue into Tasmania, we need to reset the infrastructure to greater take into account human capital, social capital, not just economic capital which is predominantly where government tends to focus. We think that we need to look at a different model of investment into Tasmanian communities that understands that there is a range of capitals that actually make up a resilient state or a resilient community. At the moment we haven't got that balance right.

**MS CHESTER:** I guess there is this broader picture in policy speak that the Commission look at and HFE is kind of one small component part of it. I'm not suggesting, given the numbers, that it's an insignificant component part for the Tasmanian budget. But it would be good to – because you have sort of painted a little bit of a picture of Armageddon from our draft report, what do you understand to be the likely fiscal impact and – even if our draft recommendations were adopted by government and implemented tomorrow, what do you understand to be the fiscal impact and how that might flow through to service standards?

**MS GOODES:** I think it would be on two fronts. Obviously in terms of the general services delivered by the government itself and particularly in health and education, we would see the biggest hit if we were to take a single dollar out of either of those systems at the moment. That's not to

argue that the dollars going into those systems don't need to be used more efficiently and effectively and potentially revisit what we would probably describe as – not necessarily the most contemporary policy approaches in some instances.

5

But the flow-on effect out into the community across a range of other parts of our service system – so like many other states and territories, our government has outsourced, to predominantly the community sector, but in some cases [the] for-profit [sector]. A large proportion of human services didn't agree. That is being delivered in a model that we would already argue is so lame that it can't be maintained into the long term to withdraw funds in any element of that, whether that's in housing and homelessness or services all the way through to just the range of emergency services that are delivered. But all our disability services, our family intervention services, many of the counselling and support and financial services that are outsourced by government to the sector would be dramatically reduced should the revenue reduce.

**MS CHESTER:** I guess, so you did have a bit of an understanding of what the fiscal impact might be – so this would be like an overnight implementation, which is not what we're recommending. Indeed, we're looking at a very – we want to have a very well-phased transition path because we do understand the impact particularly on the fiscally weaker states, that even if you were to implement either equalising to the average or equalising to the second highest state overnight – and I look at it as maybe a percentage of revenue because that's – those order of magnitudes make more sense to me than just dollars. It would be 1.3 per cent to 2.8 per cent of Tasmania's current revenue. So that's not really a material number. It's not an immaterial number but it's not a material number.

30

When I look at that and then I look at assessed versus actual expenses, it's not clear to me that it would really impact the standard of services for those assessed expenses. But I guess coming back to the point of the transition path, and that's an area where we've tried to sort of consult with the fiscally weaker states, the principle that we set out in our draft report was to say that we wouldn't want to see the fiscally weaker states materially disadvantaged by this change, particularly given our starting point with quite large relativities at the moment. So in terms of how we then look at transitioning over a longer period of time and pacing it gradually such that even a non-gradual phase – immediate phase-in would be 1.3 per cent to 2.8 per cent – what do you think would be not materially disadvantaging the state if we were to try to implement that principle?

**MS GOODES:** Well, I assume that principle assumes that the state will be able to make up that revenue through other means. My observation and our

45

- understanding is that that would be very challenging for our state, in part because of the figures we're presenting in terms of the declining number of young people who are in that sort of age bracket where we could maintain what we would consider to be the critical mass of population we would need. But equally, in terms of the State Government's capacity to address what are such entrenched levels of disadvantage, we strongly argue that no matter how staged the transition of that was, how would we take into account where the State Government would be picking up any loss.
- 5
- 10 **MS CHESTER:** Does TasCOSS have any sort of views – you touched on earlier in your opening remarks about sort of efficient – tax reform and efficient optimal taxing of the Tasmanian revenue bases. Do you have views on that, where you'd like to see taxation policy - - -
- 15 **MS GOODES:** To be honest, at a limited level, because generally the work that Councils of Social Service do at a national level is really looking more at what we're meant to be looking at federally. We would argue as COSSs collectively – and we have in a number of instances – that we actually need to have this conversation at a federal level before we can have it at a state level.
- 20
- MS CHESTER:** And that's where we kind of get to in the draft report as well where we flagged that – and it's kind of interesting. The CGC did some analysis post our draft report which shows that even with WA, with its current mining royalties, being the fiscally strongest state, even when you equalise them as the highest, they themselves can't meet their assessed expenses. So the key issue here is really not HFE, it's really vertical fiscal imbalance which is driving it.
- 25
- 30 **MS GOODES:** That's right, yes, and which is sort of our national conversation that we partner with ACOSS. I know that ACOSS present regularly on this at a range of different hearings. We would argue that we currently need to have a complete overhaul of our tax system to also understand in some of the data we've presented today the changing nature of work, the need to maintain a strong safety net in a country that is seeing a decline in fulltime employment and wages stagnating. We don't currently have a system, we think, that is looking into the future and has the vision of how we are going to move, not just this part of our tax system but our whole system, to better cater for the needs of the country where we're moving in the next 50, hundred years. At a state level we don't have and haven't done any sort of detailed - - -
- 35
- 40
- MS CHESTER:** No, that's fine.
- 45 **MR COPPEL:** I just wanted to pick up on a point you made about the

regions within Tasmania. Tasmania is a bit unique in that local governments actually provide quite a lot of community services to their community and the system we have in Australia at the federal level among the states and territories is, in part, reproduced for funding for local governments. That's based on a system which is quite different from the federal level. It's not equalising to the strongest state. It has quite a significant proportion based on the per capita basis. I'm wondering – there seems to be a disconnect – if you had any comment on that.

**MS GOODES:** Yes. My observation is that our local government system in Tasmania is quite different to other parts of the country. I know for a fact in Victoria local government delivers direct services in disability, aged care, and is quite a prominent service provider. That doesn't happen in Tasmania. Our councils vary from some councils employing community staff who work on the ground in communities, but not in direct service delivery, more in that community development space. We do have 29 councils, which is a lot of councils for a small state, and we have limited consistency, I guess, in terms of who delivers what.

So we'll get a large council in the north with limited community development input, [and a] council in the south like Hobart City Council with a strong team in that space. Again, it is one of those variables in Tasmania that it makes it challenging for us. We don't have consistency of what that looks like, I guess, across our state. What we do have though is pockets across Tasmania that in our more rural and regional areas – the east coast – often people look at our west coast and our declining employment. But actually the average household income on the east coast of Tasmania is around about \$300 less than any other parts of our state. So we have major variances in terms of the need. People move to those communities because they're generally cheaper to live in, but equally, they are the areas least serviced in terms of health or even – getting a critical mass of students to make a school at its most viable level.

It is in part – while we look like a small state, actually geographically we're one of the most dispersed populations in the country and our capacity at the three layers of government to service the needs based on our demographic profile is pretty challenging.

**MR COPPEL:** I just have one final question. You hold the strong view that the current system should be maintained. Do you have any views on within that current system changes that could be made to improve how HFE works?

**MS GOODES:** I think it comes back to the point that we were just touching on with Karen's question around being very direct and transparent and

accountable. So we would argue that we still have deficit areas of investment by state government. That's been the case not just currently but for quite a long period of time. We would argue strongly that the more accountable and transparent through that Grants Commission process that those funds are, the more capacity we have to make sure that we're targeting the right areas and that we've got the balance right between what we would call the tertiary end of our need in the system, at a particularly – health level, versus the preventative and primary areas that may mean that in 50 years' time we can turn around some of those areas of disadvantage that are currently really weighing the state down and holding us back.

**MR COPPEL:** In terms of specifics to get that improved transparency and accountability, you mentioned in your opening remarks work within the State Budget. Are there other measures that would support improved transparency?

**MS GOODES:** It's one of those areas where I'm always hesitant to say – we need to sit down and really understand what that would look like. I guess there's some concern at the moment, for example, with the legislation that's just been tabled around the national housing – of local housing partnership. So the NAHA [National Affordable Housing Agreement] is suddenly going to tie the states to a whole range of areas that may not be directly related to social housing or homelessness. So I'm always a bit wary to make comment in that regard without saying that I think potentially where we could add some value at the moment in terms of this review is potentially understanding at a deeper level what needs to be addressed – is there, ah, particular areas of service delivery. For example, affordable housing is a major issue in Tasmania and particularly in Hobart, as it is in many other parts of Australia. I don't think there's a simple answer to that question, I guess, is what I'm saying because what we often see is the unintended consequence if we don't drill that down and understand what is the problem we're trying to address, and looking at it in terms of a contemporary policy environment what would we want to do differently for that to happen.

**MS CHESTER:** We know from our own work on ROGS, reporting on government services, that there's a lot of very detailed work required there.

**MS GOODES:** That's right.

**MS CHESTER:** In terms of what might be relevant for our report though is – and this might sound like a Dorothy Dixier but it's not meant to be one. We've actually asked for the cover to be open completely on the information, data that the states and territories give the Grants Commission, their worksheets, how they do their calculations. The reason we do that is

because we've got a lot of academics that would like to roll up their sleeves and do some really good work. You might be familiar with Neil Warren from UNSW, his work in this area.

5 **MS GOODES:** Yes, I am.

**MS CHESTER:** We've got state and territory governments, some saying yes, some, including the Tasmanian Government, saying no, that it would lead to a misunderstanding of the system to allow access to that data. So  
10 it'd be good to get your thoughts on that.

**MS GOODES:** Again, I can't comment on what our Treasury does in terms of crunching those numbers and how they come up with the rationale that they do. What I will say though is – and I've said this recently in the  
15 NAHA example – the community services sector receives large grants from state government and our sector has to report on outcomes. We have to be able to provide very detailed modelling around the unit pricing models that we use to cost our services. So I do find some irony when we have  
20 governments who require that of those that they fund, but they don't want to be able to respond in an equal way when they receive funding, whether that's from the Commonwealth or anywhere else. I think there is a principled approach to ensuring that outputs, outcomes and impact is able to be transparent from a state government perspective as much as we are, as a sector, required to be very transparent in terms of grant funding we  
25 receive.

**MS CHESTER:** We don't have any other questions, Kym. Thanks very much for participating in our inquiry today.

30 **MS GOODES:** Thank you.

**MS CHESTER:** I'd like to call the next participant to our inquiry, the Tasmanian Government and the Tasmanian Treasurer. Welcome and please come and join us. Good morning, Treasurer. Good to see you again.  
35

**MR GUTWEIN:** Likewise.

**MS CHESTER:** Nice to do it in Hobart this time.

40 **MR COPPEL:** Jonathan Coppel.

**MS CHESTER:** Good to see you, Tony. Hello Anton, good to see you again. Please take a seat, make yourself comfortable, gentlemen.

**MR GUTWEIN:** Now, do you have a copy of the presentation I was  
45 planning to run through or not?

**MS CHESTER:** No.

**MR GUTWEIN:** You don't.

5 **MS CHESTER:** We look forward to it, as long as it doesn't go longer than five minutes, Treasurer.

**MR GUTWEIN:** I will get through it at a canter.

10 **MS CHESTER:** Excellent. Thank you very much. And your colleague in the Northern Territory as well. Just from a logistical perspective, can you just state name, rank and title just for the purposes of voice recognition for our colleague here. Then if you'd like to make some opening remarks with your presentation for us, that'd be great. Thank you.

15 **MR GUTWEIN:** Peter Gutwein, Treasurer of Tasmania.

**MR FERRALL:** Tony Ferrall, Secretary of Department of Treasury and Finance.

20 **MR VOSS:** Anton Voss, Deputy Secretary of Department of Treasury and Finance.

25 **MR GUTWEIN:** Karen, thank you very much. Firstly, could I just thank the Commission for coming to Tasmania. I'm pleased that you're here and that you've got an opportunity to hear firsthand from others in regards to their view on your draft report. I want to briefly discuss the intent of HFE, including the importance of HFE. I then want to talk about the scope of the Productivity Commission's inquiry on HFE, including the influence of  
30 Western Australia's current budgetary circumstances, and then discuss the key findings and recommendations from the draft report, including the strong state premium concept as well.

35 If I can move to the second slide, the aim of HFE is to equalise the capacity of state governments to provide services of a similar standard across the country. It reflects a belief that Australians, wherever they live, should have access to similar standards of service. It's a strong egalitarian principle that's been reflected in the CGC's approach in one form or another since its inception in 1933. Australians do not want to see a nation with  
40 regional disparities that exist in some other federations that protect state autonomy and enable for provisions of services to state communities reflecting specific and varied priorities to those communities. Any move away from full horizontal fiscal equalisation would reduce the level of equity between the states and territories.

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5       The third slide, what does HFE mean for Tasmania? In 2017-18 our total revenue was expected to be approximately \$5.9 billion. The state's largest source of revenue is GST, estimated to be \$2.4 billion or approximately 41 per cent. The effect of HFE is that it will deliver 18 per cent of Tasmania's total revenue. We receive 1.1 billion more than our population share and this 1.1 billion reflects the fact that per capita cost to provide an average level of services to Tasmanians is higher than the national average and that our revenue raising capacity is lower than the national average.

10       Putting this into perspective, HFE distributions represent 64 per cent of Tasmania's health expenditure, 71 per cent of education expenditure, or 100 per cent of housing, social security and welfare, public order and safety in 2017-18 terms. The Commonwealth Treasurer issued terms of reference to the Productivity Commission on 5 May. I note that he did that without any consultation with the states or territories. In our view, this was largely driven by lobbying from Western Australia, given the problems that Western Australia have with their budget position.

15       The Commission was asked to determine whether the current HFE system impacted adversely on the Australian community, economy and state and territory governments in terms of economic activity, national productivity and incentives for state revenue and expenditure reforms. The Commission was then asked to determine whether there were preferable alternatives, if any, to the current HFE system, what improvements could be achieved.

20       Tasmania considers that the clear implication of the first issue is that the Commission had to initially demonstrate that the impact of the current system of HFE has been detrimental before it could address the second and propose preferable alternatives. Tasmania further considers that if the Commission was able to demonstrate that HFE was detrimental, it would then need to clearly demonstrate that any alternatives to the current system of HFE were materially better over the longer or shorter term.

25       I might just touch on the Western Australian impact. The 2011-12 Budget speech by Christian Porter I think is very informative. The recent debate about the integrity of the current HFE system being generated by the decline in WA's share, I think when considered in the context of what Mr Porter said in respect of his 2011-12 Budget, in his Budget speech, where quite clearly he understood that there would be an impact and he set his Budget settings on the basis that there would be a floor, erroneously assumed on his behalf at that time. That has largely led to some of the difficulties that they face.

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Now, the other point that should be made in respect of WA is that through the period they benefited by about \$7 billion in additional GST from 2010-11 to 2013-14 because of the mining revenue assessment, due to the lagged approach that's taken with the assessment. I want to be clear, the fact that they find themselves now in difficult financial circumstances is not the fault of HFE or the GST distribution methodology. The lagged GST assessment, the decline in WA's share were predictable and were well-known by the Western Australian Government. The changes to GST methodology that Mr Porter forecast in that speech didn't eventuate; and for sound reasons didn't eventuate.

But what happened – Western Australia kept on spending. They chose to increase their current expenditure by historically very large rates in public sector wages and salaries and services and spending on infrastructure. Much of this increased expenditure has become structurally embedded, such that it's difficult for them to unwind. Consequently, WA now faces major challenges in respect of restraining its expenditure.

I just want to make the point that their current expenditure growth rates from 2006-07 through to 2015-16, based on actual expenditure data, was 7.3 per cent annum; significantly higher. They were 2.4 per cent forecast in their recent budget, but 5.6 per cent if you take the average across the 06-07 through to 2020-21. They had significantly high rates of expenditure growth.

Turn to the next slide, their total revenue. The point that I want to make here is that even though that their share has fallen to around 0.3 of an equal per capita share as a result of the increase in mining royalties, when taking into consideration all other income and revenues, [WA] has remained at above per capita total revenue compared to the national average. I want to make the point that in the period 2010-11 through to 2020-21 that the average per capita received in revenue in WA's case is \$10,658 per head; in the Tasmanian context it's \$10,372 per head. So even taking into account the rise and fall in respect of the GST, the total revenue on average received by Western Australians compared to Tasmanians is still high; is still high under the current system.

We would argue that HFE is working as it should. The chart that I have there, that illustrates that – the decline in WA's relativity as its own source revenue grew rapidly from the mid-2000s until 2013-14. But as you can see from the chart, the forecasts and projections indicate that their relativity will come back. Now, this is a zero sum game. At the end of the day, this will result in other states' relativities experiencing a corresponding decline and subsequent narrowing of the current divergence. We believe that this demonstrates that the current system is working well.

5 Tasmania is of the opinion that the Commission in its draft report has not proven that HFE has a negative national impact, has not sufficiently underpinned its major recommendations with evidence-heavy arguments and has placed too much emphasis on ameliorating the current budget position of WA. I'll take you through the next slide just in terms of some of the outcomes and evidence that was provided in the report.

10 The draft report found that HFE was unlikely to impact on efficient delivery of state services, economic growth and productivity or movement of labour and capital. It is difficult to prove that it impacted on potential policy reform. No evidence was produced that it impacted on efficient infrastructure development. There was no direct evidence provided that it impacted on state taxation reform, the development of revenue bases and tax rates, state policies to facilitate, restrict or tax the development of  
15 resources or state policy choices relating to resource extraction.

20 Notwithstanding the conclusion that there is no direct evidence that GST effects have played into specific policy decisions in the past, the Commission has presented two hypothetical reform cameos in an attempt to show how GST can be affected by changes in state policy. You're arguing that HFE is a potential disincentive, is, therefore, a barrier to efficient tax reform. We consider that those two tax reform cameos present an overly simplistic view of the impacts of tax reform on GST payments, which fail to take into account issues such as transitional and  
25 implementation issues, the complexity of implementing tax reforms and impacts on individual taxpayers.

30 To just move to the two main options that have been presented, I just want to point out that in respect of those two alternatives for less than full equalisation, equalising to the average of all states or equalising to the second strongest state, in both cases there's a large redistribution through to the strongest state. Our treasury modelling shows that New South Wales benefits from 2018-19 onwards and Western Australia from 17-18 onwards when equalising to the average of all states. Western Australia benefits  
35 from 17-18 onwards when equalising to the second strongest state.

40 Either alternative to the current system would leave Tasmania substantially worse off, resulting in the loss of millions of dollars of funding required for essential services. In these two example cases, \$640 million in round numbers in the first instance and around 170 million in the second over the period. I want to just touch on the partial equalisation, to the average fiscal capacity. The context, if GST distribution was based on an equalisation to the average fiscal capacity of all the states, the \$168 million loss in 2017-18 terms would mean that 1800 nurses or 1900 teachers would  
45 be unfunded, or all of Tasmania's police officers unfunded. That's 48 per

cent of our nurses, 41 per cent of our teachers or a hundred per cent of our police officers if it were applied to either of those employment cohorts.

5        Distribution based on equalising to the second strongest state, for a \$77 million loss in 2017-18 terms would result in approximately 800 nurses, 850 teachers and 700 police officers being unfunded. The strong state premium, I just want to make the point that the Commonwealth Grants Commission in its submission to your draft report expressed concern of the potential implications of the alternative options and the suggestion it would  
10        create a different playing field for the advantaged state which would attract what it refers to as a strong state premium. It's considered this would have a number of consequences that would exacerbate the fiscal strength of those other states that are treated differently to the stronger state.

15        In concluding, our state has serious concerns about the draft report. The majority of states and territories accord with our position, as do respected independent bodies, including the CGC. It appears that the only support has been received from the beneficiaries of the recommendations, which for obvious reasons doesn't surprise us. We do not believe that the  
20        Commission has proved that HFE has a negative national economic impact and we don't believe that the major recommendations have been underpinned with detailed evidence. With that, I'll draw my opening remarks to a close and do my best to answer any questions that you have.

25        **MS CHESTER:** Thank you very much for those opening remarks, Treasurer, and thank you for cantering through them at a productive pace. We might start with WA because, unsurprisingly, that was a lot of the focus of your opening remarks. I guess and in part some media reportings have mischaracterised our report as our recommendations being in some way  
30        prompted by WA's fiscal position and its budget management. A lot of the material that you went through, Treasurer, and, indeed, in your pre-draft report submission and your post-draft report submission resonates with us in terms of how we – our exposition of the WA Budget management position, the quotes from the Budget speeches, their ability to forecast their  
35        relativities. Do you have an issue with how we've presented the WA Budget management in our draft report? Because we thought it was a pretty sort of frank and fearless exposition. Indeed, it's difficult then to connect the dots to our draft recommendations, which I'll come back to in a moment.

40        **MR GUTWEIN:** Well, I would argue that if we're both in accord in respect to WA's financial mismanagement, that at the end of the day you should draw the inquiry to a close and allow the system to sort it out for them. To be frank, I'd argued – and since being Treasurer over the four years that I've been Treasurer – with the previous WA Treasurer, Mr Mike  
45        Nahan – and I'll argue with the current Treasurer, Ben Wyatt, in respect of

this. The simple fact of the matter is that WA received \$7 billion more in GST than it should have because of the lag. It set its budget forecasts on erroneous conclusions that they drew themselves. It's in a position now where it receives less GST.

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But the point that I want to make there is that in terms of total revenue, they will receive on a per-capita basis over the period from 2010-11 to 2020-21, on average, \$10,650 or thereabouts in terms of revenue per capita compared to Tasmania which is 10,300. Even with the impact of the lower  
10 relativity, they will do better in revenue terms than what this state will.

**MS CHESTER:** Let's go to why WA does matter to our inquiry and how it does relate to our terms of reference and the impact HFE may have on the real economy. With WA being an outlier – and, indeed, when we –  
15 post-draft report we wanted to get a better idea as to whether or not we thought that WA being the outlier was here to stay.

**MR FERRALL:** (Indistinct).

20 **MS CHESTER:** Being fiscally stronger than all the other states.

**MR FERRALL:** Effectively, I think you're indicating that WA is an outlier and they're an outlier in terms of their budget management; there's no doubt about that. But in terms of HFE, they're not an outlier.

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**MS CHESTER:** No, I'm not suggesting they're an outlier in terms of HFE. I'm suggesting that their fiscal strength, their fiscal position has made them an outlier, consistent with the Treasurer's metrics in terms of how much fiscally stronger they are. That's how we use the term "outlier" in our  
30 report. The reason that that matters is (1) is it a blip or is it here to stay? Our understanding from feedback from the miners, from Chamber of Commerce in WA is that it is likely to be here for the foreseeable future. Why does that matter? It matters only in a sense of it means the redistribution, the equalisation task within HFE is greater than it's ever been  
35 historically and that's here to stay for a while.

That kind of just brings me back to the key area that we wanted to discuss with you today is that I think we can all agree – and, indeed, some of our recommendations the Tasmanian Government does agree with – is  
40 that equity is the primary goal of HFE. But the CGC themselves have some subsidiary principles that they try to balance with. One that we're grappling with is the focus of our concern about the impact HFE may be having on the real economy, when the equalisation task is so great, is the one of policy neutrality.

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5 So we'd like to get your views on how well the CGC is grappling with this trade-off between the equity principle and the one of policy neutrality. I think the way we've focussed on policy neutrality, indeed the CGC does, is the impact it may have on states' decisions with respect to development activity, especially controversial development activity, and then also with respect to any significant tax reform changes. So how well do you think the CGC can do that task at the moment and how well are they doing it, Treasurer?

10 **MR GUTWEIN:** Firstly, let me just come back to the, WA and whether it's different or not. WA's own budget papers indicate that their relativities would rise. Now, the simple fact of the matter is that the Secretary of Treasury was making the point - - -

15 **MS CHESTER:** But they don't go back to historical trends.

**MR GUTWEIN:** Unless you want to argue that - - -

20 **MS CHESTER:** No, I'm just trying to get the context right.

**MR GUTWEIN:** The context is that as Australians the resources of this country shouldn't be delineated by lines drawn on a map. That's the concept of the fiscal equalisation. In terms of WA, will they receive over a longer period of time a lower relativity? Probably. But so they should. At the end of the day, as I've demonstrated, in terms of the period out to 2020-21, the average per capita revenue that they will receive in Western Australia is higher than what we will receive here. To be clear - - -

30 **MS CHESTER:** Can we just bring it back though to the implications of that, not in terms of WA's fiscal position and budget management, but the implications that might have for the trade-offs. Under the current arrangements how do you feel the CGC is faring at getting that balancing act right between the equity principle and policy neutrality, because they've got their own methodology review underway and they're trying to grapple with it already? So they're grappling with the same issue that we're grappling with.

40 **MR GUTWEIN:** My personal view – and I'll allow Treasury officials to make their points as well – I believe that the system is working very well at the moment. Again, you can't divorce this conversation and this inquiry from the fact that WA put themselves into the position that they are in. That is a statement of fact. That can't be divorced. Now, if WA had been better budget managers and if they had spent some of that revenue that they received as a result of the lag more appropriately or they had not spent that

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revenue, which is probably more appropriate, that they had ensured that they strengthened their financial position rather than continuing to spend, I don't think we'd be having this conversation. My view is that the system works very well. I'll allow the Secretary of Treasury - - -

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**MS CHESTER:** Just on that, what matters from our perspective is how large the equalisation task is within the GST core because that has implications for the trade-off between the equity principle and the policy neutrality principle. So this is quite separate to WA's budget management. I think we can agree to agree on that because it was in our report.

10

**MR FERRALL:** Why are you saying the level of distribution within the pool effectively impacts on your view of policy neutrality in this case? I don't quite understand what you're trying to get at. I mean, effectively the large redistribution is just showing that HFE is working. It's not a - - -

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**MS CHESTER:** It is working from an equity perspective. But because the equalisation task has become so great, which means - - -

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**MR FERRALL:** What do you mean by that? I'm struggling with that when you say "it's become so great".

**MS CHESTER:** So it's gone from about – it's now about 70 per cent of the pool is now redistribution across and between the states. So because you have one large outlier – I don't have the metrics in front of me, but I think we've gone from about, in a net sense, the churn is about – it was 7 or 9 per cent and now it's up around 13 per cent. So that means more is moving away from EPC. Now, we reject any suggestion – we did have a lot of submissions that suggested we go to EPC, being the view that EPC, equal per capita, meant that you had a completely neutral system. There wouldn't be perverse incentives or disincentives for some of these policy neutrality issues.

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Indeed, we've had one participant suggest let's just lock the rates that we've got today. It wasn't in WA. Thus, they don't change over time. Thus, you'd have a completely neutral system. I think it was – might have even been Vince Fitzgerald in South Australia. So that's why it kind of matters and that's what really prompted our focus on how is it coping at the moment with getting that trade-off right? Because if you equalising to the highest and you've got the highest as such an outlier, doesn't seem to be much wriggle room. You'd be aware of the CGC's recent report where their way of dealing with that trade-off is to have a draft recommendation to allow, say WA – so wherever a state effectively sets the average as WA does for iron ore – but if they increase their royalty rate then they get to keep 50 per cent of the revenue. So that's the way the CGC is trying to grapple with it.

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5 We're trying to grapple with it a little more holistically. That's why I asked the question – and it's a genuine question – how do you think the system is grappling with that trade-off at the moment and what are your views on how the CGC is trying to deal with it? Because that of itself would have implications to Tasmania's relativities going forward.

10 **MR FERRALL:** CGC continually refines its methodology and it has to grapple with those sorts of issues and it's got a proposition now which we are looking at and where CGC is seeking feedback, I think, by February next year. We'll be looking at it from that point of view, from a Tasmanian point of view in terms of the impact and whether we think it's appropriate to make that adjustment within the current CGC methodology.

15 **MR COPPEL:** Can I bring you to that specific example of policy non-neutrality, which is the iron ore assessment? We've got 97 per cent of iron ore sitting in WA taking the average – the average policy is going to be led by what happens in WA. That's why there's a recognised issue of policy non-neutrality in the CGC. Do you accept that as a specific area of policy  
20 neutrality with the current system that we have?

**MR GUTWEIN:** Before the Secretary Treasury answers that, can I just say again, that is not a good outcome for Tasmania and, again, that doesn't recognise the fact that Australians, wherever they are, the resources of this  
25 country shouldn't be delineated by lines on a map and those more fortunate than the rest of the country by virtue of where they live geographically. As a government, we will resist any change that would see any detrimental impact on the state. Now, I know that we're working through that issue that the CGC has put forward.

30 But, again, I come back to the root cause of why we're having this discussion. One state didn't manage its budget appropriately and has put itself into a difficult position. That state will still receive on a per-capita basis more revenue than what this state will, yet we're sitting here having  
35 an argument about how we can actually provide that state with more money. We don't accept that that state should be provided with an uplift. Now, Mr Ferrall wants to add something further.

**MR FERRALL:** As I said, I think that the process the CGC is going through is consistent with how it's adjusted for – or attempted to adjust for  
40 policy neutrality over a number of years. So the outcome of that will be a range of adjustments potentially. There'll be debate and argument and discussion across the states as to whether the adjustment should or shouldn't occur. I think that's quite different to the propositions or cameos that you've put forward in the report. I'm comfortable that the CGC will work  
45 through that issue of policy neutrality quite appropriately and reasonably.

We may not agree with the outcome. We may have different views. But it is able for a position of policy neutrality.

5       **MS CHESTER:** So it would be good to know what you think the impact  
might be on Tasmania. Even if you were to sort of rewind the clock and  
look at what would have happened if WA had increased the royalty at the  
beginning of the mining – royalty rates at the beginning of the mining boom  
and retained 50 per cent of the rate increase royalties. To some extent, in  
10       our draft report we rejected for the very reasons that you've outlined,  
Treasure, why we didn't think on all mining royalties there should be a 50  
per cent discount because of how fortuitous you are to have what's under  
the ground within which these state/territories lines are drawn.

15       But there are these issues of policy neutrality that the CGC is going to  
be grappling with. It's a statutory agency and it's going to make those,  
effectively policy calls themselves. Yes, they do consult with states and  
territories, but they're going to have to make some big ones going forward  
because if the WA outlier is here to stay – they're coming more to the fore  
is what I'd like to suggest.

20       **MR FERRALL:** Mining booms aren't unique. They just haven't occurred  
in the last few years. These things have occurred in the past and, again, the  
CGC has worked through those and so have all of the states and territories.  
I mean, you keep sort of throwing that WA is an outlier. I think I'd totally  
25       reject that it is an outlier in that sense. I mean, these things have occurred in  
the past; they've been dealt with appropriately through the CGC process.

30       **MS CHESTER:** And that's part of the evidence-gathering that we're doing  
at the moment. We always put out a draft report but we don't have a full  
evidence base. That's why we have a draft report, that's why we have public  
hearings and we have post-draft submissions and further consultation. But  
the evidence that we've gathered so far would suggest that the production  
levels are set at that very high level now. They are here for the foreseeable  
future, given the iron ore that's under the ground, the contracts that are in  
35       place, and it might just move around a bit according to price volatility,  
commodity prices. So from that perspective, you would envisage the CGC  
is going to have to grapple with these policy neutrality issues themselves.

40       **MR VOSS:** Well, they are grappling with these. As Tony said, we're going  
through a process. The fundamental primary objective they have – you talk  
about the policy neutrality principle. You've got a range of supporting  
principles, but HFE is the overriding primary objective. Tasmania will be  
arguing along – we're obviously still considering the proposal they've put  
up. But the issue with going down the policy neutrality suggestion that  
you've done and the draft one that's put up with the CGC is ultimately it  
45       comes back to the HFE question and you meet up with permanently



entrenching – WA in this case – or the high fiscal capacity of the other states. That is, as you say, something the CGC has got to consider as they go through that process. You talked about realigning the clock. Well, as the Treasurer said earlier, they sort of got \$7 billion over four years through that lag process. They would have got even more money through that.

**MS CHESTER:** Well, I was only making that comment in terms of understanding what the impacts were because CGC is going to be grappling with these issues going forward. Even our tax reform cameos – and we’re doing a bunch more of them on the good, bad and the ugly as more evidence base to help inform where we might land in our final report. The CGC themselves are now - - -

**MR FERRALL:** Why are the cameos evidence based – I mean, they’re clearly not evidence based because the Commission hasn’t been able to find evidence to support the cameos.

**MS CHESTER:** Well, we have had some further evidence and you’ll see those in the transcript hearings from WA and other states and territories. And that’s part of our process at the moment is to garner further evidence. So where we’re looking for what incentives might face a state or territory with a system that we kind of think is struggling because of the equalisation task being so great, we will always do modelling to get a better understanding as part of our evidence basis to what those incentives and disincentives might be.

The CGC themselves are starting to focus on this as well. Indeed – and you might have more insights than we do about this, but they’re now looking at what policy neutrality issues they are facing on the way states undertake their tax policy and tax reform with the consultancy that they’re doing on elasticities because they don’t feel that they’ve got that right at the moment. It is very difficult. Indeed, we grappled with it in our cameos as well. So what I’m suggesting is that the policy neutrality issues are going to be needed to be dealt with and the CGC is kind of heading in that direction and that’s really what motivated our draft recommendations.

So that’s why we want to get a sense of where you sit in terms of do you see this policy neutrality issues as being material, the ones that CGC is grappling with at the moment, and how comfortable are you or what are your views on the pros and cons of the way the CGC is proposing to deal with them?

**MR VOSS:** I think part of the evidence to date is that – I mean, in the past WA has raised iron ore royalties and I think in the most recent budget they found something in regard to gold royalties as well, despite the fact it would

impact on their GST. I think Tony's point around the evidence is there are so many factors to consider, as you'd appreciate, with regard to tax policy. It's not as straightforward as just the impact on the GST (indistinct).

5       **MR COPPEL:** And we wouldn't deny that. The point of the cameo is really to try and tease out what can't be teased out in the actual information that we have. There's no counterfactual but it's to illustrate that principle and we would agree that it's sort of at a lower level than if there were actual. But it does illustrate a point and it illustrates the point for the large states.  
10       We're not saying it would be something that would influence Tasmania given the size of Tasmania in the overall economy.

**MR FERRALL:** I think the cameos as presented, at best, illustrate that under certain circumstances something is theoretically possible. Going to  
15       Anton's point, it's sort of an nth order issue when you start looking at tax reform or other reforms. So simply because something is theoretically possible under certain circumstances doesn't mean that it's supportive or evidence that that is driving a particular behaviour.

20       **MR GUTWEIN:** The concern I've got with the cameos as well is now that you've stood them up I'm certain that WA and potentially some of the other stronger states may do their very best to back-fill it to ensure that the argument does stand. But the simple fact – and, again, I come back to this. The outcome of this inquiry, the Commonwealth Grants Commission  
25       process as well, we need to be very, very careful that what doesn't occur is we don't entrench the relative disadvantage that the smaller states have. Tasmania wants to be in a position where it is more self-reliant and we want to grow our own revenue base. Now, I've said publicly I wish that we had some of the challenges that WA have had in the past.

30       **MS CHESTER:** It's interesting you raise that, Treasurer, because even with WA being the fiscally strongest state – when you look at the recent – the CGC gave us a very helpful submission post-draft report where they showed that even WA – so once we equalise to the highest WA can't even  
35       meet their assessed expenses. So kind of the real driving factor there is vertical fiscal imbalance. So what position states and territories still have to - - -

40       **MR GUTWEIN:** Well, we'd like as much money from the Commonwealth as we can possibly get.

**MS CHESTER:** Well, do you want it through revenue raising powers, Treasurer, or do you want it through - - -

45       **MR GUTWEIN:** Again, there was discussion over the last couple of years

in regards to the White Paper, which, unfortunately, that discussion was curtailed and never went further. I'm not going to set tax policy here today in regards to the state. But obviously we want to be in a position where we do have a strong efficient and growing tax base. Obviously those  
5 discussions will continue. But the concern that I've got is that for a state as Tasmania, which has had a relative disadvantage to the rest of the Commonwealth – we've had to overcome the tyranny of distance and we have around 1 per cent of the footprint of this country.

10 I would hope that the outcome of this isn't that you make recommendations that would entrench that disadvantage and make it more difficult. This is one of the things I wanted to get to, as I'm sure you will at some stage. But the conversation in regards to transition paths, we won't  
15 look at any transition path because at the end of the day all that is is a transition to a point where Tasmania will receive less revenue than other states.

**MS CHESTER:** So it is kind of important though to see it in that broader context of longer term Commonwealth/state relations, because there's only  
20 so much you can expect HFE to do in and of itself in terms of - - -

**MR GUTWEIN:** True, but I come back to the point, if we're talking about Commonwealth/state relations, it shouldn't be driven by the fact that one state was the catalyst because it couldn't manage its own budget position.  
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**MS CHESTER:** Well, terms of references come to our desks in many way, shapes and forms, Treasurer.

**MR GUTWEIN:** I'm sure they do.  
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**MS CHESTER:** At the end of the day, it's more important what we do with them. Coming back to the issue that does matter the most from Tasmania's perspective, and that is the equity principle within HFE. The way that HFE – and, indeed, we touched on this earlier with TasCOSS, our  
35 first participant at this morning's hearings. The way HFE does it is gives you guys the fiscal capacity to meet your assessed expenses. But GST money's untied, you have autonomy in terms of how you spend it. So when you're trying to look at it from an equity lens we've had participants, academics, different groups representing disadvantaged members of the  
40 Australian communities, indigenous groups, look through to what actually happens when you get your GST moneys and then what actually is spent on those assisted – so what's the outcome. When you look at it for Tasmania there is a material difference across some areas that are of concern to those stakeholder groups.

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At the moment for Tassie over the last sort of six years your 7 percentage points – and don't get me wrong, we know that there's state autonomy and it's your decisions and you're making those trade-offs in your own Cabinet room. But when we're looking at it through the equity lens you're 7 percentage point short of spending what you are assessed as needing to spend in those areas of services to communities, welfare, housing, post-secondary education. Then when you look through – so schools education is the one that you actually meet the target and just go slightly above it. All the others way under; services to communities is 34.8. I guess what sort of - - -

**MR FERRALL:** So you didn't look at the revenue side? I mean, what you're using - - -

**MS CHESTER:** Revenue is relevant to fiscal capacity.

**MR FERRALL:** You're actually misusing what the HFE does in that example. The calculation isn't to indicate what a state should or has to spend in those categories. I mean, it's certainly a matter for the states to make choices. But in presenting that as you just have then, you ignored the other side, of it, which is the revenue side, where the state has a below average in terms of revenue.

**MS CHESTER:** That's why you do get that money to get you up to your assessed expenses.

**MR FERRALL:** No, but if you looked at our assessed revenue raising capacity, we raise below our assessed capacity.

**MR VOSS:** You made an example before with regard to WA can't budget because they're not getting enough. On the basis of your criteria, we are, Tasmania over the past three years on average is in exactly the same boat; we are raising less in total assessed revenue than what our assessed expenditure is.

**MS CHESTER:** Don't worry, we had the same discussion with WA and the Northern Territory.

**MR VOSS:** I'm not saying it's necessarily bad. I think you're misusing - - -

**MS CHESTER:** No, so I'm trying to understand when - - -

**MR VOSS:** Sorry. It's a theoretical construct base which they use to help them distribute GST. As you said, Australia has autonomy, they have

untied funding. But it's not like the Treasurer and Tony going to budget committee and sit down and see, "What did the CGC say?" and that's how much we spend or don't spend. It's just not how it works. Some of the detail in regard to things like services to communities or (indistinct) the other side on other revenue there's a policy choice about revenue. The government has made a range of choices in regard to how much they raise and then you've got to set that off, as you'd understand, with the expenditure side. It's just very unhelpful in many ways around saying that, "Hey, the CGC said you should be spending X amount on housing or health," or whatever and then indicating that's what the government should be doing, because that's - - -

**MR FERRALL:** Because the CGC doesn't actually say that. If you read their report that's not what they're saying.

**MS CHESTER:** We understand all of that and we understand autonomy and trade-offs in Cabinet. But in the same instance we have a slide pack from the Treasurer that says what are the implications of our draft recommendations. It's translated to some of these areas.

**MR GUTWEIN:** I think, quite clearly, the slide pack that I provided does indicate that if the outcome of this is that you take further revenue off us, then there will be those sorts of implications; as simple as that. But, again, and with the greatest of respect, the Productivity Commission doesn't make recommendations in regards to what states should spend on health or education or other services. The Commonwealth Grants Commission doesn't. HFE provides the states with a level of revenue and at the end of the day, then priorities and choices are made. I don't believe that utilising that example – and it's been utilised by others in public before, both under this government and past governments. I don't think it stands up.

**MS CHESTER:** Stands up in what sense?

**MR GUTWEIN:** Well, I don't think the point that you're attempting to make is that, based on the Commonwealth Grants Commission view of the world in regards to the revenues that you receive that you should be spending at or more in respect of those particular areas that you've raised. I think they are policy choices for governments to be taken with the full context and understanding of what's occurring in a state at that particular time.

**MS CHESTER:** That's right, and that's why it's untied money.

**MR GUTWEIN:** Absolutely.

**MS CHESTER:** We don't have a problem with that in our report, Treasurer.

**MR GUTWEIN:** Good.

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**MS CHESTER:** But it was more - - -

**MR FERRALL:** I'm trying to understand if you accept that, I don't quite understand the point you're trying to make. If you accept that it's a construct for another purpose and then you're trying to utilise it - - -

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**MR VOSS:** Similar to pay equity, which is based on a notional average level of services. You mentioned education before.

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**MS CHESTER:** Sorry, can I just respond to the first point? This is like debating, which means it's a good public hearing. No, the reason I raise it is because you're making decisions in Cabinet for the best interests of Tasmanians to not spend the assessed expenses in the way that the CGC assessed your needs in deciding what your fiscal capacity should be. You're obviously making a decision to spend it on something else. I guess is there any trade-off then with that equity principle being carried through? That's the whole reason for this question.

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**MR FERRALL:** No, but you don't make a choice in the manner you've presented to spend it somewhere else. I mean, you make a choice by – or the governments make a choice to spend the revenue they have in particular ways because it's their judgment that that is the best or most appropriate way for expending the funds for the benefit of the community. How the Grants Commission has measured or assessed the distribution of the untied funds is totally irrelevant to the policy choices that a government makes. That's the point I'm making. You're trying to conflate the two of them. One is for a very particular purpose.

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**MS CHESTER:** It's very helpful what you just said.

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**MR VOSS:** I think the other really important thing on the benchmark that you're using is a notional average service delivery. You mentioned education before. You were saying Tasmania seems to spend the right amount on an equity basis. As is known in Tasmania, there are a range of areas where our education performance has been low over a long period of time. The government has undertaken a whole range of reforms to try and lift that education outcomes because we've had a range of very poor education outcomes which feed into a range of issues with health, with productivity in the state, with wages, a whole range of issues. In this case this government makes a rational choice on an equity basis to spend more

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5 money on education than other areas. The benchmark you're using on an assessed expenditure level to determine equity is based on a notional service level average across the country but which is not what they're – Tony's point that sort of the premise you're basing it on in an equity sense – we just don't think that's valid.

10 **MS CHESTER:** That's helpful, gentlemen. Turning then to the fiscal impact, if we set aside a transition path for the moment, if we were to move tomorrow to one of our – and we only flagged that there's a whole range of different ways that you could equalise to less than the highest state. The two that we focused on, for providing some transparency around what the implications of that might be, in an immediate sense to states and territories, was equalising to the average and equalising to the second highest. In your post-draft report submission, indeed, in our report we have what the  
15 immediate fiscal impact that might be on Tasmania if we were to do it cold turkey overnight for the next year. But when you kind of step back and look at that as a percentage of your state revenues it's 1.3 to 2.8 per cent.

20 **MR GUTWEIN:** So the point being that - - -

**MS CHESTER:** So then if we're looking – we're interested and thinking of a transition path. I know you don't want to contemplate one, Treasurer. But if we are trying to implement the principle which we flagged in our draft report of wanting to ensure that a transition path ensured that the  
25 fiscally weaker states were not materially disadvantaged, where does the 1.3, 2.8 per cent sort of sit, in your view, of what's materially disadvantaged or are there other principles we should be following?

30 **MR GUTWEIN:** I'm sure the Productivity Commission has had this presented to it before. With the transition part what you're talking about is the boiling frog. That's what you're talking about. That's exactly what you're proposing is that with the transition path we won't lose all of the money upfront, but we will get to a point at some stage where we will – and we will have that embedded moving forward.

35 The concern that I've got is that in a country that's got a strong egalitarian history, culture and ethos, that if you put in place a transition path to actually take this to a point where – that you believe we can manage our revenues down over that particular period of time and our expenditures and it's a longer period to allow us to get used to it – what you will simply  
40 do is entrench the relative disadvantage and the difference between ourselves and the larger states. That's simply not fair. That's simply not reasonable. That's why from the point of view of the state we don't want to discuss and we will fight a transition path on any terms, because it simply  
45 entrenches that relative disadvantage. It just takes a little longer to do it.

5 **MS CHESTER:** Let's leave the transition path and maybe there's a couple  
of other areas we did want to touch on with you, if we may. The first one  
was in the post-draft report submission you had some concerns about our  
suggestion that the CGC would issue draft rulings to a state or territory  
jurisdiction who wanted to better understand if they were to embark on a  
major economic development activity that might have significant costs that  
they would have to expend in an infrastructure sense or if they were looking  
at doing a major tax reform what might be the implications or how it would  
be assessed or treated by the CGC. We thought that was a helpful  
10 recommendation in terms of taking uncertainty or policy chill out of the  
equation, which we've received some earlier submissions and commentary  
on from other parties. But you didn't quite see it that way?

15 **MR FERRALL:** Look, I guess our concern would be that things move and  
change significantly over time. To ask the CGC to give rulings sort of, I  
guess, a la the ATO, wouldn't necessarily take into account the particular  
circumstances of issues at future points in time. So I'm not sure it would  
actually give the certainty that you're intending to try and find by creating  
those draft rulings. I think to the extent some of them are more principles  
20 than rulings, it might work. But if they are principles, not rulings, then they  
still won't give that level of certainty. So it's really a question of what might  
happen over time, how things change and the specificity of those rulings.

25 **MS CHESTER:** We did see them being akin to an ATO ruling where –  
and having in a previous life worked on tax policy stuff at Commonwealth  
level – it has those caveats that I think you're talking about, Tony, where  
you've got your concerns. That is, that there are changes in how the ATO  
over time will interpret the law. There are changes in their regs. There are  
changes in the law. A draft ruling, as we understand it, doesn't exclude you  
30 from any of those developments. Indeed, so the CGC methodology review  
would still occur. So it is a point in time, but it's for them to get a sense if  
all the other parts of the playing field stay about the same, how are you going  
to assess it?

35 **MR FERRALL:** I mean, I suppose the other point I'd make is that there's  
generally no particular surprise for states in terms of how the CGC assesses  
particular matters. Certainly from a Tasmanian point of view, when we're  
looking at particular issues we can be pretty certain how the CGC may deal  
with a particular transaction that the state might be involved with in terms  
40 of receiving funds from the Commonwealth for capital or other matters. So  
I think there's a good understanding of that. Going to the next step in terms  
of the ruling is to give certainty, I think you must be talking about other  
matters which are very particular, which is why I say that I think it would  
be difficult, potentially, for CGC to make those rulings on a very particular  
45 matter and then for them to be applied as a ruling more broadly.



5 **MS CHESTER:** I'm very conscious of time and we've probably nearly overstayed our welcome with you, Treasurer. But I think the other area where we would like to get some help and assistance from you is you very helpfully provided some headline numbers from some projections and modellings that your officials have done. We'd very much appreciate if you'd be able to share those numbers with us, with our – at officials level because we've got projections from WA and a transition path from them. We want to do our own work. But at least the one thing we would like to sort of try to get some semblance of agreement, even with the confidence band, is under current arrangements what projections of relativities, at least for the forward estimates, might be. So if we can ask for your assistance in doing that.

15 **MR GUTWEIN:** We're quite happy to share that and work with you. As I think we've indicated to you, we have our own CGC model. But it is heavily driven by the inputs of estimates from other states in terms of their own revenues. So we don't try and project other states' own source revenue. So we take that effectively from the other states' projections.

20 **MS CHESTER:** That'd be great if we could work together. I'd much appreciate it. One more from Jonathan.

25 **MR COPPEL:** One question, which particularly relates to an area where I think Tasmania is in, at least, partial agreement with the draft report, which is the recommendation that the CGC take on a greater role in explaining how the decisions have been made and the outcomes that have dropped out of that process. So that's for improved understanding of the HFE and what it's aiming to do.

30 A second element of that was greater transparency in the information that the CGC uses to reach that outcome so that it's at a much more detailed level. It's not the sort of information that would inform the person in the street, but it's the sort of information that is used by academics, for example, the sort of work that looks at accountability issues in terms of assessed expenditure's actual outlays, but sits within the realm of looking at HFE. It's that aspect that I think you took exception to in your post-draft response. I'm wondering if you could elaborate a little bit more on your reasons why you see that aspect of improved transparency as being not a productive one.

40 **MR FERRALL:** I don't think we've said that aspect of it isn't productive. I think you've got to link that to the first part of your comment, which is about the CGC taking a role in terms of developing a better and proper understanding of effectively what it does. There's been a range of commentary similar to what you put forward earlier around the assessments in the different categories and whether a state should or shouldn't expend

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at that point. If you read the CGC's own guidelines and their own reports, they don't make anything like that sort of assertion and so there's a gap between what the CGC is doing and a clear understanding of what they're doing, and even what some academics are picking up and saying, "Well, this must mean states should spend at a certain level and if you're not, you're doing something wrong."

I think the role of the CGC can be enhanced in terms of improving that understanding and so that, I guess, less informed commentators don't make the mistake of trying to utilise the CGC methodology and information inappropriately.

**MR COPPEL:** Is that possible? I mean, when you have information sort of user beware - - -

**MR FERRALL:** Look, I don't think it's just pure user beware. I think there's always an onus on people who release information, governments that release information, to ensure that there's a clear understanding of what the information is. If you just put it out, effectively it's just data; it's not information.

**MR VOSS:** Or at least trying to correct misconceptions that might arise.

**MS CHESTER:** And that's why we've said necessarily running in parallel to the CGC playing more of an educative role so they feel they could take to task, if they wanted to, associate professors from the UNSW. But from our perspective, indeed, we thought most state and territory governments, the Australian Government, were heading in the direction of open data to allow it to be utilised by other parties and for better understanding.

**MR VOSS:** To be fair to them, as you know, there is a lot of – there's still a lot of stuff there on – if you want to get into it. I think what Tony is talking about is sort of the man in the street and the misinformation that's sometimes espoused by people who don't want to get all the detail because it's all right for us economists to get into that sort of stuff, but generally they don't. I think that's the balancing act that we're struggling - - -

**MS CHESTER:** That's okay, we wouldn't want to rely on what people said about our reports in the media to get an understanding of what was in our reports. Anyway, thank you very much. You've all been very generous with your time today and we do appreciate that it's been able to be such a frank exchange of views and ideas as we pursue the holy grail of finalising our report. Good to come to Hobart, Treasurer.

**MR GUTWEIN:** Good to see you again, Karen.

5 **MS CHESTER:** So I'd like to invite our next participants up to join us. The Tasmanian Opposition Labor Leader to join us, thank you, and Shadow Treasurer. Good morning, welcome, thank you for coming. Good to meet you. Thank you very much for joining us this morning. Once you've had a chance just to make yourselves comfortable, if you wouldn't mind just each stating name, rank and title for the purposes of our voice recognition, although if they confused yours that'd be problematic. And if you'd like to make some brief opening remarks. We'd like to keep those to up to five minutes, if that's at all possible.

10 **MS WHITE:** That's fine. Thank you. I'm Rebecca White, leader of the Tasmanian Labor Party.

15 **MR BACON:** Scott Bacon, Shadow Treasurer.

20 **MS WHITE:** Firstly, I'd just like to thank you very much for coming to Hobart and providing an opportunity for a hearing to be had. It is an issue that Tasmanians feel particularly passionate about, as you've just witnessed from some of our presentations. At the outset I'd just make the statement that the Labor Party in Tasmania does not support the change to HFE as consistent with our presentations and submissions that we've made to you. We're not making that argument because we don't think there should be economic reform, it's just that there hasn't been any evidence presented in work that's been provided to date that demonstrates change to HFE is in federation's best interests and certainly not in Tasmania's best interests.

30 Tasmania has a track record of good economic and tax reform. I know that's been presented to you by the Government in their submission. In our submission we did as well. I'll just note some of those things. So we have undertaken reforms in the electricity sector, reforms to water pricing, governance arrangements relating to the commercial activities of government businesses, deregulating shop trading hours in 2002, taxi industry reforms in 2003. Together with Victoria, Tasmania was the first state to meet its targets to abolish inefficient state taxes as part of the 1999 Intergovernmental Agreement on Federal/State Financial Relations. We were also one of the first states to develop harmonised payroll tax arrangements.

40 Just recently the Labor Party has announced a policy to introduce points of consumption tax for gaming products to assist to fund some of the government activities here in this state. So we do continue to be supportive of tax reform and national tax reform specifically. It is disappointing that any tax review recommendations weren't ever pursued. But one of our concerns about the current Productivity Commission inquiry is that it is occurring in the absence of a wider debate about tax reform for the nation.

Arguments over HFE have become a distraction, really, for any real effort to make state taxes more efficient, more harmonious or more competitive. Perversely, any change to the GST that would negatively impact Tasmania, as proposed by the draft report, would actually increase the state's reliance on inefficient taxes like payroll tax, stamp duty and land tax, and act as a disincentive for tax reform at a state level.

In addition to the loss of about \$1 billion in revenue that's been forecast through the modelling that's been done by the report provided, it would devastate our ability to deliver essential services, health and education. We already as a state face challenges delivering those core essential services. We have very disparate population, an ageing demographic. We are commonly told we're older and sicker and poorer than other states across the country. That does mean that we have a particularly heavy reliance on public services like health and education.

A loss in GST, our ability to deliver on our obligation to support our people would be diminished. So we don't want to see that happen. We don't want Tasmanians become second-class citizens. I think, as the Treasurer eloquently put as well, we are an egalitarian society, Australia, and we pride ourselves on that and we don't want to move away from a model that currently supports all of our citizens to access the same (indistinct) and level of services no matter where they live in Australia.

It's good to see here in Tasmania at least all sides of politics coming together and we share the same view on this; that we don't want to see change to HFE that would disadvantage Tasmania or leave us worse off. And confusions about the model and perceptions around CGC are not well-founded as a basis for change. The argument that you've made around misunderstanding, for how it works, does not provide strong evidence for there to be then a change in the distribution model. The arguments made by Western Australia do not propose that this be the solution to their problems. There are other ways to deal with their particular issue at this point in time that does not disadvantage the rest of the country, particularly Tasmania.

I do note that in the submissions you've received the South Australian Government, the Victorian Government, the governments of the ACT and the Northern Territory and various business and community groups in those states, as well as community groups here in Tasmania, have all raised concerns about the recommendations of the draft report. Our final message to you, Commissioners, would be that we'd certainly welcome a debate about national tax reform, but please don't abandon the system that has served our federation well for decades.

**MS CHESTER:** Thank you very much for those opening remarks and thank you also for the post-draft report submission that we've received from you. We might just kick off first with what I guess we can all agree on, indeed – that within HFE, that the primary policy objective of HFE is about equity and providing states with similar fiscal capacities. The way that that's evolved over time by the CGC, instead of it being able to provide a standard of service that was not substantially lower or similar, has now become one to the same standard. Indeed, looking back through the history it's quite revealing that that was never decided by any Cabinet or any government legislation, state, territory or Commonwealth. It was actually decided by the CGC, a statutory agency.

But the CGC also in deciding what HFE should be, that it's now to the same standard, did also identify some subsidiary principles that they tried to get the balancing act right with equity. The one, and, indeed, sort of the primary one that we've focused on in terms of what could be the potential economic impact of HFE as it's currently practised on the Australian economy is around policy neutrality. So it would be good to get your views on, to what extent you feel the current system can handle that trade-off between equity and policy neutrality.

**MS WHITE:** Can you give me an example of policy neutrality so I can better understand that concept?

**MS CHESTER:** Yes, sure. The two key streams are really around where one particular state might set the average, so WA with iron ore, Queensland with coal. They might face perverse incentives about what they do with that development activity or how they might tax it because of the way the HFE system works. So there's ground development activity. Then the other stream is around tax policy and tax decisions. So these are areas where the CGC is sort of grappling with this trade-off. Indeed, their most recent methodology review second report, I think it is, has some recommendations as to how to deal with it, including discounting by 50 per cent any royalties that a state or territory may raise from an increase in the royalty rate for a royalty base, a revenue base for which they effectively set the average. So again, iron ore for WA or coal for Queensland. It would be good to get your sense of how the system is grappling with that trade-off at the moment.

**MS WHITE:** My understanding is that the 2012 review found that there wasn't a disincentive for states to pursue policy decisions that worked to the benefit of their state but to the disadvantage, I guess, of federation in their distribution.

**MS CHESTER:** I think you're referring to the Brumby, Carter and Greiner

review. They identified in principle or theoretically that those disincentives exist, but they struggled to find an evidence base. We've had states and territories suggest to us that there is a reverse evidence base, to the extent that some states and territories may not dare greatly and do development activities that might be controversial and they're effectively cross-subsidised by the other states that do those development activities through the HFE. With respect to the tax reform stuff, we did run some cameos just to get an idea of what the counterfactual would be, given we don't have a counterfactual.

**MR BACON:** We think fundamentally any of the scenarios that have been put forward that make Tasmania worse off in terms of GST payments would make it more difficult for Tasmania to reform their budget or to put forward any meaningful economic reform. I think we've shown, even from opposition, that we're willing to talk about tax reform. Rebecca mentioned the point of consumption tax for online gaming. I mean, there's no doubt that's going to become a national tax. We've seen the government here in Tasmania over the last four years effectively say there'd be no changes really to taxation. They've now put forward a policy for the next election to say they won't introduce any new taxes or increase any taxes. But we've shown a willingness to introduce a tax that we don't think will have a significant effect on any Tasmanians, but would raise additional revenue that we could put into government services.

**MS CHESTER:** How much revenue would that gaming tax you're talking about - - -

**MR BACON:** We've got modelling that, based on the South Australian experience, it would raise some upwards of \$3 million a year. We've committed from opposition to introduce that tax. We're more than willing to have a conversation about tax reform, as Rebecca said, particularly at a national level. We think it really needs to be driven by the Federal Government if we are going to see any meaningful reform. But fundamentally, if Tasmania has got less GST we find it hard to believe that it would be an incentive for us to undertake major tax reform or rely less heavily on inefficient taxes. We just think that any of the scenarios that have been put forward would make it more difficult, not provide an incentive to do those things.

**MS CHESTER:** Setting aside just Commonwealth, state and vertical fiscal and balancing tax issues – we will come back to that – do you have a view – does the Labor Party have a view as to whether or not Tasmania is getting best bang for buck out of its revenue bases at the moment in terms of ultimately taxing those revenue bases and raising as much revenue as possible but without discouraging economic activity?

5 **MS WHITE:** Well, it's a hard one to be able to provide you with a comprehensive answer from Opposition, to be honest, without the resources of Treasury. But there are a number of inefficient taxes that have been identified but they're not new taxes; they're existing taxes. However, to reform them would require a fundamental change to the way that we tax a lot of those things that are economic drivers of the state. There's a lot of challenges to overcome, I suppose, before you would tax some of those things.

10 **MS CHESTER:** From your perspective, tax reform at a state level needs to really be part and parcel of a broader Commonwealth slate...

15 **MS WHITE:** Well, Tasmania was one of the states that got rid a lot of the inefficient taxes when the GST was introduced. But there are very few taxes or revenue raising abilities that we have compared to other jurisdictions, where they've maintained continued use of some of those taxes. For us, we don't have many options necessarily; we've only got a few limited options to raise revenue as a state. That's why we are so dependent on the GST and why any change to it would be so devastating for us.

20 **MS CHESTER:** We'll come back to fiscal impacts in a moment. But in terms of if we were to look at them, in that, down the track with the broader lens of changes to vertical fiscal imbalance – because I'm not sure if you were here earlier but we talked about even – WA, as an outlier in a fiscally stronger state at the moment, even they at their fiscal capacity can't meet their assessed expenses, which is a function of vertical fiscal imbalance or they're not doing the right thing by their own tax bases at the moment. So what would you see as being any change in taxing powers Commonwealth/state to facilitate Tasmania having a better fiscal capacity and being able to sort of look at doing some home-grown tax reform?

25 **MR BACON:** We certainly would be keen to participate in those discussions. But we think that the inquiry at the moment in terms of distribution of the GST shouldn't be held in isolation of a broader national discussion around tax reform. It's really difficult for Tasmania as such a small state really to push ahead without any leadership at a federal level. We think that at the moment while that conversation is not going on, there shouldn't be any change, in particular, to the way that the GST is distributed.

30 **MS CHESTER:** We sort of say in our draft report that, "Look, there's only so much we can do in the confines of HFE in and of itself." That to do any more sort of holistic reform to Commonwealth–state federal financial

relations would require issues like vertical fiscal imbalance to be considered. So we do sort of acknowledge that. I guess what I was interested in was, what do you see that that might look like to allow you to sort of be able to contemplate having a greater fiscal capacity for Tasmania and to be able to sort of embrace any state-based tax reform.

**MR BACON:** We'd say almost you'd need to look at that, if not in conjunction, then before you look at any change of distribution to the GST. We think it's almost – you've got things around the wrong way effectively, that there should be that national conversation rather than just talking about the GST and only putting forward scenarios where Tasmania will be worse off. It gives us less incentive. All it does is unite effectively everyone in Tasmania at a political level against any changes rather than getting people talking about what is possible on the other end. From our point of view, the situation where it is at the moment, we agree – we heard some of the comments that the Treasurer made. But effectively there's nowhere in Tasmania that can support any change at the moment and there's no way you can even get people to have a conversation about changes to state taxation or to vertical fiscal imbalance until you effectively take this off the table.

**MS WHITE:** I know you're very limited by the terms of reference that you were provided and obviously you've got to make your inquiries based around the terms of reference. But I think that's the biggest problem for us, as the Shadow Treasurer has outlined, is that the terms of reference are very narrow in scope and it does limit the ability for us as a nation to have a conversation about all the other things we do need to be talking about.

**MS CHESTER:** I think our biggest constraint is something called the zero sum game, but anyway.

**MR COPPEL:** Rebecca, you mentioned in your opening statement that there are other ways of dealing with the problems with HFE today. Can you explain to us then what you see as those problems and the solutions that represent other ways?

**MS WHITE:** The reason why we're all in this room and the reason you are touring the country is because Western Australia is crying poor because they're not receiving GST that they think they're entitled to. They, because of the lag effect, benefited from GST and the mining boom at the same time. Whilst from a period of about 2011 it was forecast their GST would decline, they've clearly failed to plan for that and now they find themselves in a situation they are. Can't also hide away from the fact that there's politics at play here where there are seats in Western Australia that the Liberal Government wants to win. So they're playing to that audience too.



5 There are ways to deal with Western Australia's problem in isolation without dismantling HFE. The Labor Party at a federal level has identified additional money that could be provided for infrastructure to assist that state government to deal with some of its fiscal challenges and obligations to its people. They are decisions that can be made at a policy level by Canberra politicians that deal with the current problem Western Australia has, without impacting and disadvantaging other states and smaller states like Tasmania.

10 My recommendation would be that – my hope would be that your report back to government demonstrates that there's an unwillingness across Australia, not just from small states like Tasmania but from some of the larger states like Victoria too, to dismantle HFE and that in order for the government to deal with the political problem it sees in Western Australia  
15 it needs to find another way.

**MS CHESTER:** The problem with that is that that's not our motivation. Our motivation is actually how well the system is getting that trade-off between equity and policy neutrality. So a top-up from the Commonwealth  
20 effectively just increases the effective relativity that WA gets. It doesn't change the incentive issues and the policy neutrality issues that is the focus of our inquiry.

**MS WHITE:** You can't deny that that's what's precipitated the inquiry and it's an issue – a problem Western Australia will soon find resolved  
25 anyway because it will swing back the other way and they will receive more GST under the existing HFE model. So they will soon start to benefit more because of the existing model that supports the rest of us.

30 **MR COPPEL:** In our terms of reference we were asked to examine what impact HFE has on state/territory budget management, which everyone is pointing to the example of WA. Our conclusion was that HFE is a sideshow to that. The experience of WA is management. What we've identified, I  
35 guess, as a specific area which does relate to WA is the subsidiary principle of policy neutrality which does come into conflict with how HFE works in the case of the mining royalty assessment for iron ore where the average is dictated by one state, given the nature of where the resource lies.

40 That's an issue that's been identified also as an issue with the CGC review of its methodology. It's proposed for discussion a discount on the marginal increase in revenue from an increase in the royalty rate as one way of minimising or muting that impact. It too boils down to less than full equalisation or partial equalisation. Do you see policy non-neutrality in that specific example as a problem? Do you have any views on the proposal  
45 that's been put by the CGC to at least go some way to addressing that issue?

**MS WHITE:** That would be for the mining royalty discount?

5 **MR COPPEL:** Well, it relates most pertinently to mining royalties, but that's framed in a slightly broader way.

10 **MS WHITE:** My understanding is that if – say we be specific about a mining royalty discount. But even in that scenario Tasmania would be left worst off to the tune of about \$42 million in just one year. So even under that scenario Tasmania loses because of policy decisions that are being made in Western Australia. So I do still have problems with that, obviously. I'm not sure if you've got anything.

15 **MR BACON:** I can only agree effectively.

20 **MS CHESTER:** Sorry, \$42 million, that's a straight discount, whereas the CGC is just looking at – just so you're not mischaracterised when the transcripts are read by others, that that's for – and that's something that we recommended against in our draft report. We didn't agree with having a broad mining royalties discount because we think that that breaches the equity principle of HFE. The CGC themselves will make a decision and they've got a draft on the table which says if WA or any state or territory that effectively sets the average increases the royalty rate they get to keep 50 per cent of what they raise from that increase. So that in and of itself would have implications because it's revenue that then is not assessed as part of the HFE.

30 **MS WHITE:** No, and not available to redistribute to smaller states like Tasmania. Have they done modelling around what that could look like?

**MR COPPEL:** It would be in the CGC documents.

35 **MS WHITE:** I don't feel I could make a comment on that without seeing the detail.

40 **MS CHESTER:** But that's kind of what we're grappling with. The CGC within their own sort of way of viewing HFE will make decisions as they go in terms of how they will grapple with policy neutrality. We've come up with recommendations that probably deals a little more holistically. But I think the policy neutrality issues are here to stay.

45 **MS WHITE:** Yes. For things like mining extraction though when you are part of a federation, those mineral resources belong to the whole nation. It's fortunate for Western Australians that they are obviously in Western Australia and they can benefit as a jurisdiction from that. But the reason

we're part of a federation is that we do share our resources and what can be extracted from the ground and we share in the benefits from that too. So I would have trouble – and Australia, not just Tasmania, if one state was able to benefit more from the fact that they sit on a mineral deposit and don't share that equitably, if there were changes that disadvantages other Australians because they don't live there.

**MS CHESTER:** So that's kind of why we landed on not supporting – what a lot of people, including the Minerals Council, put to us was to just discount mining royalties across the board. The flipside though is if you are state or territory government and you're looking at doing a development activity and particularly one that might be controversial, you're going to wear the political pain but you're not going to get all the revenue gain. We still need to have the overriding principle of equity but we need to be conscious that that in and of itself could deprive the development activity, which then all states and territories would stand to benefit from the royalties that would come from it. These are the sorts of policy neutrality issues that we're kind of grappling with, not WA budget management.

**MS WHITE:** I mean, you're right, it's a national issue.

**MS CHESTER:** So it's how that might impact on the real economy is kind of the heart of our report. They're all the questions that we had for you.

**MS WHITE:** Thank you.

**MS CHESTER:** Is there anything else that you wanted to say before we hear from our next participant who is a national treasure in Tasmania, Saul Eslake?

**MR BACON:** We fundamentally don't think that the case has been made for any change to the current system. We see the issue in WA as a one-off outcome to assist them. It has stood the country in good stead for a long period of time. So we just don't think the case has been made for any change.

**MS CHESTER:** Thank you very much for appearing today.

**MR BACON:** Thanks for coming down.

**MS WHITE:** Yes, thank you for coming to Hobart.

**MS CHESTER:** I've already hinted at who our next participant is. I'd like to welcome Saul Eslake to join us. Just make yourself comfortable, Saul. Saul, thank you very much for joining us. Just for the purposes of the

transcript recording, if you can just state your name and who, if anything, you represent. Then if you'd like to make some brief opening remarks. I'm conscious of time. If you could keep them to up to five minutes. And cognisant that we've read everything you've provided and said in the public record. So it'd be good if you could sort of focus on anything that's new.

**MR ESLAKE:** Thank you. My name is Saul Eslake. I'm an independent economist. I'm also a vice-chancellor's fellow with the University of Tasmania and a non-executive director of Hydro Tasmania, but I'm here in a personal capacity and not representing any of those or any other organisations. Thank you for the opportunity to be here and to comment on the draft report. As you said, you've seen my submission and other things that I've said. So I guess I kind of summarise it by saying I'm not here to say that the system of horizontal fiscal equalisation is perfect or that it shouldn't be changed in any way.

But what I would say is that, in my view, the draft report has not persuaded me, at least, of some of the conclusions that it's stated. In particular, it hasn't persuaded me that the system is broken. It hasn't persuaded me that full equalisation is not an objective which should continue to be pursued. It hasn't persuaded me that there is, in any material sense, perverse incentives that discourage state governments from pursuing worthwhile economic or taxation reforms, or foregoing worthwhile economic development opportunities.

The report seems to accept the fact that, a vast majority of Western Australians regard the outcomes it's been delivering in recent years as unfair, as sufficient evidence to back away from the objective of full equalisation. It hasn't established any principled reason as to why something less than full equalisation ought to be pursued and all of the options that it has presented thus far are essentially different ways of deciding who should get less so that Western Australia can get more.

In my view, notwithstanding the difficulties that Western Australia is currently experiencing, they are, nonetheless, by many relevant measures the wealthiest people in Australia as a group. Almost all of the Commission's recommendations, in effect, require cash to be transferred from the governments of states and territories which are poorer than Western Australia to the government of Western Australia so that, as the Grants Commission has put in its submission to you, Western Australia can enjoy a kind of fiscal premium relative to the rest of Australia.

I said at the beginning that it's not my position that the system is perfect or doesn't need change. But what I would have thought would have been more consistent with the terms of reference that you have is to ask whether

there is anything about the way in which the Grants Commission goes about achieving full equalisation that has detrimental effects on economic activity, productivity or any of the other things that are considered worthwhile. If it's established that they do, for example, in the analysis which you provide about the different treatment of changes in tax rates from changes in the basis of taxation, which was a point I hadn't previously considered, if you've established that full equalisation could be pursued in simpler, more transparent, more predictable ways or pursued in a way that would tangibly enhance economic efficiency, then the recommendations that might flow from that are far more likely to be acceptable, irrespective of their impact on what each state and territory receives.

**MS CHESTER:** Thank you, Saul. That was incredibly efficient, Saul. Thank you very much. Just at the outset and just so we don't perpetrate any mischaracterisation of our report and very conscious that some people will read what's in the media and interviews that people have and can sometimes misconstrue what's in our report, our report explicitly says the system is not broken but we feel it's struggling a little bit with where the equalisation task has gotten to. We say that equity has to remain the primary objective as it is currently. We say what's happened in WA has eroded confidence, but we attribute that more to the lack of accountability and the lack of understanding of the current CGC model, thus, our very frank exposition of WA's budget management. Indeed, we drew on some of your previous work on that, Saul.

Just so people don't read articles and mischaracterise our report – indeed, I met with one other silver-haired gentleman who's an economist that I greatly admire recently and he'd only read that article and said, "What the heck are you doing?" Then when we talked this person through what we'd actually done in our draft report his view changed. Anyway, I just want to make sure that the mischaracterisation couldn't be attributed back to you, Saul, so I thought that was important to be read in the context of what your opening remarks were.

I guess coming back to the key issue here is how well is the HFE system currently performing? What impact might it have on the real economy, which was kind of the guts of what we were asked to do? You yourself say, I think in everything we've read, that you've told us, your opening remarks, that the system is not perfect. It does need some fixes. What do you think are the current flaws of the system and what are the fixes that are required?

**MR ESLAKE:** Let me answer that, first of all, by saying that the fact that the system is currently producing outcomes which have no historical precedent is not in and of itself evidence that the system is, I think the words that are used in the report even, under strain.

**MS CHESTER:** We'll come back to that because that is a key issue. But just in terms of what you think are the problems and what you think the fixes are.

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**MR ESLAKE:** I think the problems are partly, as the report has diagnosed, that the system is poorly understood. Very few people outside state treasuries and part of the federal treasury and the Grants Commission itself understand how it works. It relies to a very great extent on judgments by the Grants Commission which are hard for outsiders to replicate. The outcomes can be variable from year to year, which make the management of state and territory budgets harder than it would otherwise be, although I'd also note in saying that comment that, for example, volatility in stamp duty revenues in particular can have a similar impact and in some cases a bigger impact on state budgets than changes in GST relativities from year to year. So that of itself is not necessarily an argument against it.

Finally, and your report has been influential in my own thinking about this, there are some anomalies in the way the Grants Commission arrives at its findings regarding fiscal capacity and the use of fiscal capacity from the different ways in which the Commission treats, on the one hand, changes in tax rates and, on the other, changes in the base of state taxation, which, although you didn't provide, because I don't think there is any, evidence that that's been a serious obstacle to state governments making those sorts of decisions in the past, it, nonetheless, could quite easily result in – may have resulted in states either being treated unfairly from some kind of objective standpoint or not pursuing desirable reforms such as the one you canvass of replacing stamp duty with land tax, of which I've been a very long-standing advocate.

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I don't think that the possible impact on GST revenue is a reason why no state government has done that up to this point. But it obviously would be a consideration. I'm also an advocate of in Tasmania lowering the rate of payroll tax and applying it to all businesses; broadening the base, lowering the rate. And I infer from the analysis that's in your discussion of the stamp duty land tax, that that might also have problematic implications for Tasmania's GST share. So those kind of things, which you would approach not by saying, "Let's step back from full equalisation and see what happens," but rather, "Let's look at the way in which the Grants Commission actually goes about achieving full equalisation and see what happens."

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I think that's an approach that would be much more consistent with your overriding objectives of seeing whether the system has any adverse consequences for productivity, economic efficiency, economic growth and

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so on than saying that the trade-off between equity, on the one hand, and efficiency, on the other, ought to be shifted in the direction of efficiency, which is, in effect, what you're saying by recommending something less than full equalisation.

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**MS CHESTER:** If you look at some of our options in terms of what might be a way of equalising to less than the higher state, it's because that equalisation task becomes so large and, as you'd appreciate as an economist, that as you move away from EPC you do start mucking around with incentives that states might face. And we reject moving to EPC because that completely abrogates the equity objective.

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**MR ESLAKE:** And I would even question whether EPC should be used as a benchmark. I know it's an easy benchmark to use. But given that grants have never been carved up among states and territories on an EPC basis, given that state governments themselves don't distribute money within their jurisdictions on an EPC basis, but rather, on the basis of some perception of need - - -

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**MS CHESTER:** I think they do with local councils though.

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**MR ESLAKE:** No, they - - -

**MS CHESTER:** Some state and territory jurisdictions do, so their version of HFE for their local council is very close to EPC.

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**MR ESLAKE:** My understanding is that with local governments they distribute 70 per cent on an EPC basis and 30 per cent on an equalisation, on an HFE basis, and they all have state grants commissions in order to recommend that. Even with that money they don't distribute it on a pure EPC basis. But accepting that it is, as you say – I mean, the federal government tax transfer system doesn't distribute money among the population on an equal per-capita basis. We accept that some people are going to be significant net contributors to the system and some people are going to be net withdrawers from the overall tax transfer system.

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While there may be some adverse consequences for efficiency arising from the fact that 3 per cent of taxpayers pay 30 per cent of personal income tax, nobody seriously argues that that should be used as a reason as to why that same 3 per cent of taxpayers should pay say 20 per cent of personal income tax.

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**MS CHESTER:** I think we can agree that we do not see EPC as an equity benchmark for looking at HFE. But for some it could be seen as an efficiency benchmark. But the whole ballgame here is really, equity is the

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primary objective. Policy neutrality or efficiency is a subsidiary objective. How do we get the trade-off right within the system without eroding to too great an extent the equity objective? How do you think the CGC is going at the moment, Saul, in terms of getting that trade-off right between policy neutrality and equity?

**MR ESLAKE:** Well, what I say is that the existing system of HFE, combined with the spatial effects of the federal tax transfer system, have created a situation where the degree of inequality across Australia is substantially less than the degree of inequality you can observe in other federations. Now, a large part of that is because of the way the federal tax transfer system works. But, as your report, like many others beforehand, acknowledge, Australia goes further in the pursuit of HFE than almost any other federation.

I'd argue that we do that because we can, and the reason we can is because our federation is characterised by much more vertical fiscal imbalance than almost any other federation and it's the vertical fiscal imbalance which, in effect, determines how much is available for HFE. So I think it is something to be proud of rather than something to regard as prima facie grounds for questioning the system, that there is less inequality across Australia regionally than there is in many other federations. While the system has been delivering those outcomes under more challenging circumstances in recent years than previously, Australia, nonetheless, has achieved better overall economic growth than many other countries and has increased its per-capita standard of living relative to most other federations.

So I'd argue that it's hard to point to any significant efficiency or economic cost that Australia as a whole has suffered because we have pursued HFE to a greater extent than other federations.

**MS CHESTER:** HFE today now has a much greater equalisation task within the GST core because we do have an outlier.

**MR ESLAKE:** Yes.

**MS CHESTER:** So that means we're further away from EPC. You do agree though that EPC is kind of like an efficiency benchmark but not an equity benchmark. So you don't see that there's any policy neutrality issues at play at the moment across the Australian economy with development activities or tax?

**MR ESLAKE:** I think you make a case that there could be in terms of the different treatment of rates of taxation versus the base of taxation. What you, like others who've investigated this before, have been unable to come



up with is any evidence that what might be true in theory has actually occurred in practice. I struggle to believe that any state has foregone economic development opportunities or worthwhile reforms purely or predominantly because of concerns as to what that would mean for their share of GST revenues. I have seen even here in Tasmania, for example  
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**MS CHESTER:** And we don't say that in the report, Saul, either, just so it's not mischaracterised.

**MR ESLAKE:** No, but others have said it to you.

**MS CHESTER:** But if those disincentives are material and decisions are always made at a margin, how can you expect a state or territory government to dare greatly with a controversial development activity or dare greatly with a tax reform of the kind that you and I and Jonathan would like to see if they are perversely penalised by the GST relativities?

**MR ESLAKE:** Because there's neither evidence, nor can I recall in the Tasmanian context or, for that matter even, given I lived there for 30 years, in the Victorian context a government ever saying that although we recognise this particular proposal is something that would be good for the state that would create jobs, that would generate revenue, that might generate export income, we're not going to go ahead with it because it will have some impact on our share of GST revenues. I mean, this state government here, for example, was at potentially some – not the present state government, previous state governments have been advocates of some quite controversial development proposals. I'm thinking here about the pulp mill, for example, or, on a smaller scale mines on the fringes of national parks and wilderness areas, which - - -

**MS CHESTER:** And we say in our report the smaller states that disincentive effect is so muted because they are smaller states. It doesn't really influence the GST relativity. So it's really the larger states.

**MR ESLAKE:** So let me turn that around the other way. With the possible exception of attitudes to uranium mining, which in Western Australia come and go, depending on who the state government is, I'm not aware that any Western Australian government has held back from developing any of that state's resources for fear of an adverse impact on its share of the GST. I'm not aware that the Northern Territory has, where perhaps the incentive effect might be even greater, held back from supporting, encouraging the development of natural resources in the territory because of a fear that it might have some adverse impact on the very large proportion of the share they get of the GST.

**MS CHESTER:** I think we can all agree it's difficult to have evidence of a counterfactual and thus, like good economists, we try to then model through cameos or other means what the incentive effects are that they face.

5 **MR COPPEL:** If I come back to the question that Karen raised, do you see EPC as an efficiency benchmark?

10 **MR ESLAKE:** It's a simple one to use, but whether – I'm not persuaded that equal per capita necessarily represents efficiency. It represents simplicity, but does it represent efficiency in the economic as opposed to the accounting or commercial sense of that term? I'm not sure that you can make a persuasive case one way or the other. It's simple, but I think that's all it is.

15 **MR COPPEL:** Isn't it founded on the basis that the outcome can't be influenced by your own decision, it's a per capita – like a head tax.

20 **MR ESLAKE:** In that case, for example, would you say universal basic income is the efficiency benchmark for a social security system or a tax system or a poll tax is an efficiency benchmark?

25 **MS CHESTER:** We're looking at it from the perspective of policy neutrality, Saul, from policy neutrality from the state and territories' perspective. There's two suggestions we've had about the efficiency benchmark. One is you just set the current relativities in concrete and you never change them, because then whatever a state does cannot affect it. But we know that that completely abrogates the equity objective. The other efficiency benchmark is EPC and how far you stray from that gives you a suggestion of what the trade-off might be. We do not recommend going to  
30 EPC for the very reasons that it does undermine the equity objective.

**MR ESLAKE:** I think all I can say is that it is something that you might use to establish a boundary but that's all.

35 **MR COPPEL:** Earlier you said that maybe there are alternatives to equal per capita. Do you have something specific in mind as that benchmark?

40 **MR ESLAKE:** You could, for example, have the revenue as a percentage of gross state product would be another possible boundary definition.

45 **MR COPPEL:** This is an area where previous reviews, including by the CGC, have looked at sort of broader indicators as a way of getting simplicity and policy neutrality even. But it's always been concluded that it leads to unequal outcomes or outcomes that stray too far away from where we are at the present or where analysis was undertaken. But we've asked

in the draft report for – we’ve encouraged the CGC to continue examining whether there are those sort of broad indicator that could be used as a benchmark. I’m a bit doubtful, given the past work, how fruitful that will be. But we’re not giving up yet, so to speak.

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**MR ESLAKE:** I haven’t explored what this would mean for either outcomes for individual states and territories or for the system as a whole. But it may be, for example, that you could simplify the assessment of revenue disabilities or capacities by focusing on three or four heads of revenue and doing everything else as a proportion of gross state product. So you might explicitly look at payroll tax, stamp duties, land tax and mineral royalties, and all other revenue you just looked at in terms of gross state product as an indicator of revenue raising capacity.

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On the expenditure side, you could perhaps look at education, health, public transport and maybe law and order as sort of key areas of state responsibility and do something similar to what the Grants Commission does at the moment and then simplify the treatment of everything else. As I say, I haven’t attempted to work out what doing something like that might mean in practice and what consequences it would have for state shares. But if you started out from an objective of making the system simpler, easier to understand and, from one perspective, carrying greater accountability, that might be a way of going. You still have full equalisation as the policy goal, but the way in which you get there may, in the end, mean a different distribution of revenue from what you currently have.

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I mean, what constitutes full equalisation is, to some extent, in the eye of the beholder, if I can put it that way. It is what drops out of the myriad of calculations that the Grants Commission does at a micro level. Over time, over the history of the Grants Commission, those calculations have got into finer detail and become more complicated and thus more opaque to anyone who is outside the system who can’t really replicate what they do. For example, as I think I’ve said in some of the things, it surprises me in some ways, given that on broad economic indicators Victoria is now a relatively poor state in terms of per-capita gross product, per-capita household income, that it isn’t what the Western Australians would call a recipient state, that it’s still a donor state.

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How you get to that income is, I suppose, mainly on the expenditure side of the way the Grants Commission goes about its process. But I guess the point I’m trying to make is that a more fruitful attempt to manage the trade-offs between equity and efficiency in the HFE system might come from thinking about how the Commission achieve full equalisation as opposed to questioning whether full equalisation ought to be the objective.

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**MS CHESTER:** Just coming back to this issue of grappling with the trade-off between equity and efficiency, which I think we can all agree there is a trade-off, the CGC is doing that in parallel at the moment with its own methodology review, Saul, that you'd be more than familiar with. One of the potential changes that they're thinking about is, in terms of the royalty rate issue, would be to allow a state that sets the average – WA on iron ore – to keep 50 per cent of the revenue streams from any increase in the royalty rate. So that, to me, is sort of kind of like a way of trying to deal with that policy neutrality issue. It would be good to get your thoughts on that.

**MR ESLAKE:** My instinctive reaction to that is that that's just a different way of giving WA more money. I mean, the reality is that the tax base which Western Australia has, if it's properly defined, is not something over which the Western Australian Government has any great influence. As I think I said in a different context, they didn't put the minerals there. They don't put the capital up to develop them and neither, for that matter, do most individual Western Australians. Most of the capital that's developed their resources has come either from interstate or from overseas. The prices that are paid for those resources are determined on international markets, not by any conscious policy choices by the Western Australia Government.

So if through no particular circumstances of their doing they have the capacity to raise far more revenue from the rest of the country – raise far more revenue from exploitation of their mineral resources than any other part of the country, it's not obvious to me why any part of that should be excluded from the determination of fiscal capacity, which is what applying a discount in effect amounts to. I don't want to misquote you here, but I think your report rejected the idea of applying either discounts to particular types of revenue a la the Canadian approach or putting floors under a state's GST shares, which is equivalent of putting a cap on everyone else's. I think I would apply the same framework to thinking about the suggestion that they get a discount for any revenue that comes from an increase in the rate of tax they apply to mining royalty – rate of tax – mining royalty rate they apply.

**MS CHESTER:** We didn't comment on the CGC one because their report came out contemporaneously with our draft report. So you haven't mischaracterised us on those other issues. But I guess the CGC do see it as a policy neutrality issue similar to, I think, the coal, sea and gas. They're treating it like gambling and taking it out so you get rid of what some might claim to be a perverse cross-subsidy from those states that are daring greatly and doing coals and gas and those states that aren't being effectively cross-subsidised.

**MR ESLAKE:** Yes, although my impression – and this is an issue that's

come up in Tasmania, of course. But my impression is that the decisions that state governments have made about coal and gas have got nothing to do with either the revenue they would get from them or whatever impact that might have on their GST shares.

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**MS CHESTER:** Which raises the issue about whether or not it even breached the materiality threshold and therefore come into play, which is kind of interesting in and of itself. But you can see where we're going here. But the CGC is starting to grapple with these policy neutrality issues as they see them, but dealing with them in kind of like an ad hoc piecemeal way.

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**MR ESLAKE:** I suppose my response to that would be, as I've suggested in a different context, that maybe the issue that is really critical here is the difference in the approach the Grants Commission takes to changes in tax rates from the approach that they take to changes in the tax base.

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**MR COPPEL:** The CGC uses discounts quite frequently as part of the decisions they make in undertaking their calculations and they'll do that when they are not fully confident that their assessment is a reliable one. So in a sense it's an extension, what they're proposing, to the current practices. You've made the point that any discount is, by definition, going to be a departure from full equalisation. But if you take that strictly any change from what we have at the moment will be a departure. If I listen to you, you would rule out our – based on that immediate fact that any change is going to lead to a different distribution. We're in the zero sum game; some win, some lose.

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**MR ESLAKE:** Yes, it's obviously anything you do is a zero sum game and we all understand that. But what I'm saying, I think, is that full equalisation is, in effect – what is full equalisation? What dollar distribution of revenues is consistent with full equalisation? Well, the answer to that is whatever the Grants Commission says it is. The Grants Commission has changed its formulas, what it includes, what it excludes, what it discounts, what it doesn't over a period of time. But the result that they present has always been characterised as full equalisation.

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What I'm saying to you is that there may well be different ways of achieving the goal of full equalisation, that come out with a different dollar distribution of revenues from that which comes from the present system, but are arrived at through processes that have different effects on incentives, if there are any, that may be simpler and easier to understand and explain, that may be more easily replicated by outsiders to the process, to – approximated by outsiders to the process and perhaps more predictable by state treasuries who have to live with the consequences; and you could still describe those as full equalisation.

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5 So I guess the most important point I'm trying to make is not that there should be no change to the system at all, not that it's perfect, but that the pursuit of what would be accepted by the public at large and participants in the process as full equalisation, even though it resulted in a different dollar distribution of numbers, could perhaps be achieved by a different process from the one that is used at the moment.

10 **MR COPPEL:** Are you making a distinction between the process and the methodology - - -

**MR ESLAKE:** I'm using process and methodology interchangeably.

15 **MS CHESTER:** It's an important point that you make there, Saul, by saying what is full equalisation is what spits out of what the CGC does. Indeed, when we started this inquiry we thought history was going to be important, that history might reveal – and you've read the report fairly closely. We do run through the evolution of how the CGC has equalised and how it's been described as becoming full equalisation, but requiring fiscal capacity to be able to provide the services of the same standard. Did we get that evolution right? Because I'm still struggling to understand, the current CGC Act doesn't require them to equalise to the same standard. There's been no decision by a government or a Cabinet to provide a fiscal capacity to get them to the same standard. It's just something the CGC just decided to do.

25 **MR ESLAKE:** I mean, what my understanding is, that the CGC seeks, as they say, to recommend a distribution of revenues that allows each state by equal effort to provide its citizens with a similar standard of public services.

30 **MS CHESTER:** No, it's the same standard.

**MR ESLAKE:** Same standard. Yes, my apologies, same standard.

35 **MS CHESTER:** It used to be similar but they changed it.

**MR ESLAKE:** Was that in the mid-1980s?

40 **MS CHESTER:** Well, they started doing it back in '81 but they didn't actually say that's how they were doing it in a public record until about 14 years later. If WA hadn't have happened, that penny wouldn't have dropped with me. I always assumed that they were equalising to an average. But when you realise they're equalising to the highest we don't sort of go back through the history and realise it's just something they decided to do.

45 **MR ESLAKE:** If you go back further into the history, as you demonstrate,

of course, states could choose whether they wanted to be part of the process or not by being claimant states or withdrawing from claimancy. Sometimes withdrawing from claimancy was held up as proof of superior economic management.

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**MS CHESTER:** But that's a decision by a state or territory government.

**MR ESLAKE:** Yes.

10 **MS CHESTER:** I guess what I'm trying to draw out here is to make sure we did get that history right, given you know this history better than we do. That it is quite bizarre that a statutory agency just decided in a policy sense how we were going to do it. It's different from what's in their Act and it's different from how it was done historically.

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**MR ESLAKE:** And in the same way, as you'll know, that around the early 1980s the basis for comparison changed from the standard states, as it used to be called – Victoria and New South Wales – to the average of all states. Again, that was a decision that I think was, in essence, made by the Grants Commission rather than by the federal parliament or anyone else.

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**MS CHESTER:** Does that kind of then make sense from a governance perspective? These are big policy decisions and we now realise the cost of that policy decision as it's played out with a fiscal outlier like WA. It's made the equalisation task much greater than it would otherwise be.

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**MR ESLAKE:** Well, let me unpick that a bit. I'm not sure what the cost of full equalisation is or whether it's significant. The fact that Western Australia has become an outlier in terms of what the system produces is a direct result of the fact that Western Australia is an outlier in terms of how wealthy it is.

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**MS CHESTER:** I'm not disagreeing with you on that. But in terms of it – we're struggling with policy neutrality and efficiency and the equalisation task is much greater within the GST pool. Assuming we have an evidence base that we can further establish that suggests that there could be real cost to the economy of that occurring – do you see where my logic is going?

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**MR ESLAKE:** I mean, if the evidence base was so strong that there are efficiency costs, surely you would be able to point to something.

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**MS CHESTER:** Well, that's why we have draft reports and public hearings and post-draft report submissions.

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**MR ESLAKE:** I think you're the, as I understand it, third inquiry that's

looked at this because your predecessor, the Industry Commission, did one in 1993 and Messrs Brumby, Carter and Greiner did one in 2012.

5 **MS CHESTER:** And the previous two were slightly more constrained than we are, but anyway.

10 **MR ESLAKE:** But they weren't able to come up with any evidence. With due respect to Messrs Brumby and Greiner, given everything they had said about the system with their former hats on, you would have thought that if there was any evidence that supported the arguments that they used to put as premiers of their respective states, they would have found it and put it in their report.

15 **MS CHESTER:** Well, they didn't have the cameos. I'm very conscious of time and I'm meant to be chairing this, which means I'm doing a very bad job.

20 **MR COPPEL:** Can I just pick up the last point that you made? You've made that point that there's insufficient evidence to justify changes to the system. The other point that you make is that the changes that are proposed in the draft report don't address particular problems. Which of the two – do you give equal weight to those or which of the two do you think you hold with a strong conviction?

25 **MR ESLAKE:** I would put a stronger weight on seeking to find ways of achieving full equalisation, whatever you define that to be, in ways that are simpler, more transparent, easier to understand and more predictable. Because, as I say, I go back to the point that full equalisation is what the Grants Commission says it is and otherwise it's sort of a bit hard to define  
30 what it actually is. I mean, you can say there's that principle that each state by equal effort can, in theory, provide the same standard of public services or similar standard of public services as the average of all states. No one really knows what that means in practice. It's very hard to define beyond –  
35 yes, conceptually you know what it means, but in practice what does that mean about how big classrooms should be in one state compared with another or how long is an acceptable waiting list for acute hospital care in one state compared with another. No one attempts to define that.

40 So we sort of accept that full equalisation is what the Grants Commission says it is and the response of states who feel aggrieved by that is to say that we should pursue something less than full equalisation. New South Wales and Victoria have always argued for equal per capita. Western Australia used not to do that when they were a recipient and now they've argued either for equal per capita or floor or a discount for mining but they  
45 want to step away from the objective of full equalisation.



5 The point of view that I'm putting to you, from a sense of someone who's always interested in economic reforms that will produce benefits for the country as a whole, is not to question the objective of full equalisation but to question how we get to that objective and what it might actually mean.

10 **MS CHESTER:** One more quick question because you're a bit of a state budget guru, what do you consider would be the kind of variants that the Tassie Government would typically have around some of its key revenue measures? How much bouncing around do they have in their forecasts and what can they sort of wear without it sort of impacting standard of services that the budget can deliver on, Saul?

15 **MR ESLAKE:** Well, I'd calculate it, as you know, that an equal per capita distribution would force Tasmania either to double its state taxation revenue or - - -

20 **MS CHESTER:** Stepping away from HFE for a moment, just in the normal course of the state government doing its budget management, they don't always get their forecasts right around their revenue basis. What sort of variants do they currently have with their forecasting abilities around their revenue basis? I know that's up or down.

25 **MR ESLAKE:** That's not a calculation I've done. But my impression is that the own-source revenue side of Tasmania's budget has been less volatile than that of many other states because the economy has been less volatile. In particular, stamp duty revenue will have been lower on average but much less volatile than the states that have had pronounced housing and property market cycles. Likewise, employment has been pretty flat here compared with the growth that has occurred in other states. Land tax revenue never shows much volatility because it's the most predictable form of state revenue. The other area of volatility in revenue for the Tasmanian Government is in the revenue it gets from its GBEs because the electricity industry, which is the largest component of those, is very volatile, particularly given that sort of hydrology of Hydro Tasmania.

40 But, of course, from Tasmania's point of view with something like 60 per cent of its revenue coming from Canberra year by year movements in the GST revenue share are probably the bigger source of uncertainty from year to year in constructing the state budget. I don't know whether you've spoken to the Tasmanian Treasury yet or not. That's a question they'd be much better placed to answer than me.

45 **MS CHESTER:** I just wanted to get a sense because even if we were to sort of cold turkey to one of our proposals, the impact, when you look at it

in terms of as a percentage of state revenues is 1.3 to 2.8 per cent. I'm just trying to get a sense of order of magnitude as to what they would have to deal with in a normal budget management perspective and whether that would - - -

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**MR ESLAKE:** I put a table estimating that in my submission to you. I took the dollar numbers from, I think, four of the options you canvassed and said what was that as a percentage of revenue. Equalisation to the second stronger state was, I think, about one and a half percent of revenue for every state, except WA, which got a lot even out of that. I mean, Tasmania could live with, could accommodate, changes to the GST sharing formula to the cost of 77 million. That wouldn't break the state; they could cover that. It might be more problematic for the Northern Territory, for example. That's not to say I think Tasmania would regard it as an acceptable outcome or one that they would desire – and it's not for me to speak on behalf of the Tasmanian Government anyway. But it wouldn't break the state. The consequences of that will be far less serious than an equal per capita distribution which, again, I accept is not what you recommended but is often used as the benchmark.

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**MS CHESTER:** No, it's just a lot of people are portraying that we're recommending as kind of Armageddon.

**MR ESLAKE:** It isn't. I mean, the other option which wasn't in your report but was in the CGC submission on your draft report was, in effect, going back to the claimant state arrangements whereby you equalise among the four smaller states and territories and leave the big four states out of it.

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**MS CHESTER:** Yes, that was an interesting post-draft report submission, not commenting on policy was their opening statement. I think we've run way over, but it's been very helpful, Saul. We appreciate you being very frank with us and being generous with your time and helping us with this inquiry. So thank you for appearing.

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**MR ESLAKE:** Thank you for listening.

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**MS CHESTER:** Folks, I know we're running late, but we do need to take just a five-minute break for those of us that haven't been able to enter or exit the room for the last few hours. So we're going to take a five-minute break. We'll resume at 10 minutes past 1. Thank you.

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**ADJOURNED**

**[1.07 pm]**

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5 **MS CHESTER:** We're going to resume our public hearing here in Hobart before it starts bucketing rain. I'd like to welcome our next participants from the Launceston Chamber of Commerce. I've been to Launceston many times. Thank you for travelling down here for our public hearings in Hobart today. If each of you could just state your name and organisation just for the purposes of voice recognition for the transcript, that'd be appreciated. Then if you'd like to make some brief opening remarks.

**MS HEALY:** Janine Healy, treasurer of the Launceston Chamber of Commerce and former president.

15 **MR GROSE:** Neil Grose, executive officer at Launceston Chamber of Commerce.

**MS BAIN:** Donna Bain, voluntary director of Launceston Chamber of Commerce, former president.

20 **MS CHESTER:** If you'd like to make some opening remarks.

**MR GROSE:** Yes, thank you very much and thanks for holding the hearing in Hobart. We do appreciate it. It wasn't initially on the schedule. So we do appreciate that and we do appreciate the chance to contribute. It probably won't be to the depth of my predecessor. I guess therein lies what we want to talk about, is the practical implications of any adjustment to GST, particularly downwards. Tasmania, for better or for worse, does rely on that strong and reliable and predictable GST flow from Canberra. We've seen in the past, particularly in the previous state government, when GST revenue dropped, not by proportion but by dollar amount, it had a significant and ongoing impact on the Tasmanian community and the business community. We saw lots of cuts in health. We saw lots of cuts in community. That has an impact, an undeniable impact, on business confidence. Tasmania is a state which really does rely heavily on business confidence. We are certainly in an upswing at the moment with business confidence and in great part some of that is driven by some vision and investment by state government. Some of it is federal government. But a lot of that is always in partnership with the state government.

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Now, our concern is that if there is a significant and radical drop in GST revenue, then that ability of the state government to contribute to that growth wanes. I can give you a very brief example. It's a small one. In the northeast of Tasmania, a depressed little town called Derby, was an old mining town. It basically had 30 people living in it and about 50 dogs. But

it was recognised as a world-class venue potential, for mountain biking. With investment by state government and partnered by the federal government and local government, we now have a world-class mountain biking venue there which brings 30,000 visitors a year to Derby. But more  
5 important than that, it's created between 40 and 50 ongoing and permanent jobs. So that investment by government has transformed that very marginal regional economy.

10 There are many, many other ways that we rely upon the state government to contribute to our economic growth, probably more than any other state. As a chamber of commerce, we'd probably be the last organisation that would say that government cannot improve its financial performance in terms of expenditure and revenue. Revenue is one of those  
15 issues, for a Tasmanian government in particular, where we are limited. Our hole in the ground is a lot smaller than Western Australia's or anyone else, as is our capacity to exploit that. The change in the Tasmanian economy is moving away from that primary industry based economy, apart from agriculture. But certainly in terms of mining and, to a certain degree, forestry, our reliance is now on a new economy.

20 It's worth pointing out that Tasmania has the fastest internet speed, available in Launceston and Hobart, of anywhere else in Australia. We've got 65 per cent of our community is connected directly to fibre. We have so much potential and it's already showing in that growth in technology and  
25 professional services, which is all intellect based. There's no scope for the Tasmanian economy, I hope, to tax that. However, when it comes to mining and forestry in particular, it's a declining opportunity for the state government.

30 In the northeast in the '90s when the forestry industry was at its peak there was a million tonnes of forest products coming out of the northeast, all which was subject to royalty. Even though the forestry industry has bounced back, that's still only at about 300,000 tonnes. It will never ever  
35 get back to that scope. So there's not that capacity for the state government to say, "You know what, we've just lost a whole bunch of GST revenue, let's see what we can increase in royalty." There just isn't that scope.

I guess the changing nature of that economy is reflected in the membership base of the Chamber of Commerce. We're Australia's oldest  
40 chamber and we can plot the changes in the economy and the business make-up right back to 1849. Our membership base now is probably 40 per cent in that professional services, whether that's accountants, marketing, change people, that intellect base. If you went back 50 years ago it would have been in a manufacturing base. If you went back a hundred years ago  
45 it would have been in a mining base. So we see that change.

Now, mining and manufacturing and that primary production is a source of revenue for government. Where we are at the moment there's not that scope.

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**MS CHESTER:** Thank you very much for those opening remarks. It is good that we get a perspective from chambers like yourself in terms of how the economy in Tasmania is evolving. Indeed, my first inquiry when I joined the Commission four years ago was on the Tasmanian freight and shipping. So I spent a bit of time up the north. I guess my initial question is a little bit about – and we all do acknowledge that the fiscally weaker states are very much more reliant on the GST revenues as they're distributed through the HFE mechanism. Does the chamber have views on how the Tasmanian Government actually spends those GST moneys that they get?

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**MR GROSE:** I think certainly over the last four years we would see that the government has been very wise in the way they spend that money. They've looked to projects of infrastructure rather than just spending it for the sake of spending it. Their long-term legacy projects, Derby is probably one example, there are a range of others. There's assistance to technology. There's manufacturing hubs. There's the expansion of the university. That is a key one. That goes across all three corners of the state. Launceston at the moment is the beneficiary of a city deal which is bringing \$260 million investment to Launceston; \$60 million of that is state government investment.

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So we would say that the state government has been incredibly wise in that, but also they've used that revenue to repair our health system and our emergency services system. We've seen a rebuilding of the health system. On the broad brush, there's more nurses, there's more doctors, there's more hospital beds, but also has improved the structure of that. We also see that with the police force. So we've seen more police on the beat, which makes everyone happy, but also in the other emergency services field, which people don't often see until they're in trouble, which is the fire service, State Emergency Service and other volunteer organisations.

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**MS CHESTER:** Because I guess people sort of equate the HFE with the principle of equalising fiscal capacities with an equity outcome, and with an equity outcome is where are those dollars spent? That doesn't determine whether that's still an equitable outcome; it depends on how well they're spent and whether they're the right priorities. But when we kind of look then as to – and, as you'd know, the states and territories have autonomy with how that – it's not tied funding. But the CGC goes through this incredibly complex and elaborate process to determine what Tasmania's assessed needs are across areas like schools education, post-secondary

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education, health, housing, welfare, services to communities, roads and transport.

5           Then you get the GST money. Then when I look at what Tassie actually  
spends – and these are CGC numbers over the past six years – they’re  
actually 7 percentage points below what they’re assessed in terms of their  
expenditure in those areas. That may mean that they’re just doing it more  
efficiently or they’re getting better outcomes. But in the areas that you’ve  
10       identified as the priorities – post-secondary education, health, services to  
communities – they’re way under the numbers that the CGC assesses as  
your needs once they’ve taken into account disabilities like remoteness,  
aged population, all the rest of it.

15           So I’m just – we have people saying any change, even if it results in a  
1.3 per cent change to our GST as a percentage of our revenue, will result  
in these incredibly inequitable outcomes. But then when I kind of look at  
how it’s working at the moment it doesn’t transfer through to how the  
CGC assesses what those needs are in terms of where the money is then  
20       spent. I’m not suggesting that that in and of itself suggests inequity because,  
again, it depends on value for money, priorities and all the rest of it. But is  
that - - -

**MR GROSE:** Yes, I guess it’s probably a far more complicated question  
than my small brain can cope with. In terms of the GST revenue, it provides  
25       certainty for ongoing things which need a level of stability such as  
education. We need to know that we’ve got enough teachers to staff our  
schools. We need to know that we’ve got enough nurses. The CGC process  
is about infrastructure building, so the main road on the Midland Highway  
is that Grants Commission type thing and other iterations of that. There’s  
30       a whole range of projects going on around the state or about to start around  
the state which bolster that up.

          But that ongoing revenue stream, the GST side of things, that is the  
fundamental underpinning of how government services provide. They can’t  
35       rely on a grant to run a school system because you need that consistency.

**MS CHESTER:** Indeed, we recommended not making any changes to the  
way they do the averaging over sort of the three-year history and then a two-  
year data lag. So there is greater predictability for the states to manage their  
40       budgets knowing what those relativities might be over time. But I guess  
we’re kind of looking at well, if we in our final report do recommend any  
changes, one of our issues would be developing an appropriate transition  
path and being guided – and we only identified one principle. There’s  
probably other principles as to how you sort of manage transition path to  
45       implement a change.

One of the principles that we articulated was that a state and territory jurisdiction that's fiscally weak like Tasmania would not be materially disadvantaged.

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**MR GROSE:** In a transition – and all business copes with transition. You cope with revenue going down, you cope with shrinking business and you cope with expanding business and how you manage that. In a government sense, a transition – and I heard the Treasurer earlier saying he was utterly and utterly opposed to a transition period. In practical terms, we support that. We don't see there should be a transition. But a transition has to be a managed and staged – the worst decisions that governments ever make are when they're in distress. We saw those decisions made when GST revenue dropped four, five, six years ago, when all those decisions were made to impact on the health system and close wards and do that.

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The ongoing impact of that we will still suffer from for 20 years hence. I know that wasn't a horizontal fiscal equalisation issue. That was just simply we didn't have enough dollars. But it's still the same impact. It's still dollars into the economy. Any transition has to be strategic. So if there is to be a transition – and we would argue that there isn't – the lead time to that has to be enough so that government can not only make the right decisions but take the community along with those decisions, because the last thing you need is for government in Tasmania to become unstable because of decisions made outside of Tasmania.

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One of our foibles is the Hare-Clark system, which means that, by and large, we have an inherently unstable political system where we often end up with a hung parliament. From a business point of view, things tend to slow down. We don't like to see that. If, for example, the precursor to going back into that situation was a funding arrangement contrived outside of our control, that would be a bad outcome in terms of strategic planning for Tasmania but also in actual practical outcomes on the ground.

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It wouldn't be fair to Tasmania or Tasmanians to say that GST revenue is going to drop in two years' time. I don't believe that's enough time for such a diverse economy and an economy that relies heavily on government investment and government support. It needs to be much, much longer. I mean, there's the old rule of thirds in Tasmania. There's a third are dependent on the government, a third work for the government, a third are in private industry, but probably two-thirds of that private industry depends upon government for their private industry. The impact of reducing structurally Tasmania's access to GST funds has impacts far deeper than many would realise.

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**MS CHESTER:** If you were here earlier you would perhaps heard me say what percentage of Tasmania's revenue – if we were to cold turkey and do it overnight, it would be a 1.3 percentage point or 2.8 percentage point reduction in revenues.

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**MR GROSE:** And that would have a massive impact on Tasmania; there's no doubt about that. I mean, 2.8 per cent doesn't sound like a lot, but in terms of a dollar amount it's a huge amount. That is a ward in a hospital. It is a mental health program for youth. It is do we reinvest in a technology hub? Do we support community into breaking out of being a community like Derby, which were utterly dependent upon social security; now they're a strong, vibrant private enterprise community which is standing on their own two feet. Do we do not that? It will cause so much dislocation within the Tasmanian economy that the shrinkage in the economy will be far greater than the 2.8 per cent you would get from GST. It would compound.

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**MR COPPEL:** I just want to come back to a point you make in your submission about the criteria that you use for what would represent an appropriate distribution of the GST. You've got factors in there like predictable, fair, transparent, accountable and reasonable.

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**MR GROSE:** Yes.

**MR COPPEL:** Can you give us your assessment of how you see the current distribution process measuring up to those criteria?

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**MR GROSE:** Well, we can only compare the situation now with the situation we've always been used to. So it is our status quo. Our cloth has been cut to that. In terms of Tasmania as a whole, we'd always like to see more money. But from a business point of view, we'd like to see that more strategic. But in terms of the balance, the way it's done, we can always argue whether there should be more spent on school, more spent on medicine, more spent on a whole range of things. But by and large, the current government has done a very good job in distributing that for the betterment of Tasmania and Tasmania's economy, but more importantly, its community. To have a strong business community you need a strong community to start with.

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**MR COPPEL:** Just getting back to one of those criteria was reasonable. What do you mean specifically there?

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**MR GROSE:** Well, reasonable always depends on who's being reasonable. Reasonable, from our point of view, is that the balance is probably right. So we wouldn't want to see that balance changed. I mean, business would always like to see more infrastructure that businesses can

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leverage off to grow. But the balance is right. We have a unique community in Tasmania – we’ve got all the broad brush things. We’ve got a small population, we’re an island state. That stretch of water is our advantage but it’s also our massive disadvantage.

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We’ve got the nation’s most regionalised population and also the nation’s oldest population. I mean, part of that is because we’re a beautiful place to live but it’s also because we’re a cheap place to live too. And we’ve got the highest rate of disability in the nation and we’ve probably got Australia’s second or third worst health outcomes. You have to balance that against what else you’re trying to do with that money.

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**MS BAIN:** I think to pick up some of the earlier remarks we made today, I think our opportunities to strengthen the transparency and accountability of the system, a system which is so important to not only the integrity of the nation’s finances but integrity of the state’s finances, ought to be better understood for a range of reasons. One, it makes those decision-makers more accountable and allows the stakeholders in the system, e.g. Launceston Chamber of Commerce, to actually understand how governments make decisions and how those decisions play out in communities, because in small, reasonably diverse communities like Tasmania, as Neil has said, the impact can be disproportionate.

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It looks and feels perhaps larger than it would be in a state of, a population of 6 million, where a decision almost literally disappears in the noise. A decision like that here in Tasmania has an extraordinary impact. So issues tied up with social licence become very critical for business decision-making because everybody here will have a view about how that plays out in their community. So I think there are opportunities for government and the Grants Commission to spend much more time explaining what it is they do and how they do it and that comment earlier around the information which is fed from this jurisdiction into that decision-making process and back, we need to understand how that works, because if we are to influence what that looks like today and how we think that plays out in the future we’re going to do that on an informed basis.

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So we are all grappling with the fact that this is a very strange black box into which a whole bunch of stuff goes and then magically something appears at some stage and we wonder where it comes from. That has an impact on our capacity to have a think about what that might look medium and long term, because the last thing, as Neil just said, we want is to make decisions which are reactionary and short term, because otherwise you actually end up spending more money trying to fix that stuff, in fact, if you don’t get it right the first time. Sometimes you spend more time and effort trying to do that than if you’d actually done it properly in the first place. So

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I think this process does trigger the need to do that in a much more transparent and accountable way.

5 **MR COPPEL:** In our draft report one of our recommendations where I think there's more or less universal agreement is that the CGC take on a larger role in explaining what they're trying to do and how the decisions they reached have been reached.

10 **MS BAIN:** Because as Mr Eslake said, those decisions and that conversation you had around the policy framework, which the Commission seems to have stumbled into, is that an informed policy decision? To what extent have the people in this room and elsewhere in this community had a say in how that conversation is played out, because it plays out in the detail of the money that comes back to this state. So it's very important for us to  
15 understand how that works and to have a very strong opportunity to have a say in that policy framework.

**MR COPPEL:** How would you get there? Do you have any specific ideas on how you would create that dynamic?

20 **MS BAIN:** Well, Tasmania has a fairly strong community engagement strategy. We have mechanisms in which we can engage our local communities. Having people like you down here starts that conversation. We prepare information which people can readily understand and you  
25 engage with the local community about who they are, what they do and what their expectations are of that process. And that dialogue continues. I think in that conversation, as Ms Goodes said earlier this morning, you do have conversations around the inclusion principles which guide this state.

30 As other speakers will probably talk about, the clean and green philosophy which underpins part of this state. It gives this state an opportunity to say, "Actually, this is how we want to run our jurisdiction. These are the principles under which we as a state want to operate." It's around giving business a fair go, we'll be clean and green when we do that.  
35 We'll be inclusive. We engage the community and allows us to do that.

At the moment we're doing that in bits and pieces. But I think this is an opportunity we need, to have this say at this level, not just at the state or local level where those decisions are played out. That takes some time.  
40 You need to allow enough time to do that and to be respectful of processes and that needs to be (indistinct) because stuff will fall out of that which none of us have anticipated. That's the fun bit, to be honest, because you learn stuff about how communities react.

45 **MR COPPEL:** Thank you.

5 **MS CHESTER:** That's all of our questions. Apart from me saying I'm looking forward to coming back to Launceston next year because I discovered another great business up there, the pinot noir shop; they have an annual event. Thank you and safe travels. I'd like to call our final participant in our hearings in Hobart today from the Tasmanian Chamber of Commerce and Industry, Mr Michael Bailey to join us. Welcome.

**MR BAILEY:** Thank you for coming.

10 **MS CHESTER:** Well, we put the offer on the table, you get four participants, we will come. You topped us by two.

15 **MR BAILEY:** That's good, you've done well. Look, it's kind of depressing being last because you hear what other people say and realise that there's not much left on your list that you can actually talk about.

**MS CHESTER:** That's okay, we're running late, but we're keen to hear if there's anything further you want to share with us.

20 **MR BAILEY:** Really, I think just to extend of - - -

**MS CHESTER:** Sorry, before we do, if you could just say your name and organisation for voice recognition, otherwise he's going to throw paper planes at me.

25 **MR BAILEY:** Fair enough too. Michael Bailey, the CEO of the Tasmanian Chamber of Commerce and Industry. Certainly from the Tasmanian Chamber of Commerce and Industry's perspective, the HFE system is one that holds the federation together. It's a system that has over  
30 30 years of, I suppose, precedent that's established it. Clearly as business lobbies we always argue that the government can spend money in better ways than they do. We always argue for efficiencies and for different ways of doing things. I've got to say that this government is working hard in that space but also is looking at different ways of attacking some systemic  
35 problems in our state; issues of health and education are prime ones.

40 Previous speakers have spoken about our health issues, our education issues, which are among the worst in the country. In fact, I think on many of those measures we are the worst. So we need to do things differently in our state. We also have different issues such as freight – which impact the way we can actually hit export markets and even hit mainland markets – which are quite unique to our state in many instances.

45 We feel as a state that this whole argument has just come about because of Western Australia's mismanagement of their once-in-history opportunity

to take advantage of a mining boom. That played out very clearly in the media here with comments about us being a mendicant state, for example. What's frustrating for us is that at this point in time our state is really on the path to a much more sustainable economic future. Our indicators are looking good, exports are growing, employment is growing and we're looking at education and health in different ways.

For us, it seems a particularly unhelpful time to be talking about a review of how GST is actually managed across the country. As a chamber of commerce, we'd argue that if we need to look at tax, let's look at tax, let's look at a GST increase, for example, rather than fiddling with the system to try and appease the larger states who seem to be miffed that the smaller states have had a better run because of our (indistinct) economic times.

From our point of view, this seems to be almost a frustrating diversion from getting on with improving our state. As a community, we're all very focused on doing that.

**MS CHESTER:** Thank you very much for those opening remarks, Michael. Maybe we'll start off where you left off, which is around tax reform. That's what I was trying to get my notes – so just setting aside, apart from the GST rate increase, which I'll make very clear for the transcript was suggested by you and not by me, just looking first at state-based taxes. From the chamber's perspective, are there reforms that you would see from an investor confidence, business perspective?

**MR BAILEY:** Yes, there are and we've argued for those pretty strongly. There are only really a couple of taxes that we can look at. We understand in our state we can't take a tax away without replacing it with something else. Ideally I'd love to wish away payroll tax, for example, which I think in any state is a crazy tax, particularly in a state like ours where we're trying to grow employment. We've argued for things such as looking at a reduction in payroll tax or at least passing it to all businesses, albeit at a much smaller rate. At the moment it's capped - - -

**MS CHESTER:** So broadening base, lowering rate.

**MR BAILEY:** Indeed, which may be fairer, or looking at broadening land tax to include all land holders, rather than just business owners and shack owners, as a way of compensating for reductions in payroll tax. Again, we'll continue to argue for those. But fundamentally, government and governments before that have all agreed that these things need to be looked at. In fact, there was a tri-partisan committee formed to look at taxation in Tasmania that just became increasingly difficult. It becomes politically

5 very hard. The previous speakers from the Launceston chamber put it very well, that we do have a third of our market unemployed or on some sort of benefit, a third of our market who are employed by government in some form and a third of our market who are in business, which makes political change actually really difficult because the first two-thirds quite often can be very resistant to change.

10 So our government needs to move carefully, without kind of stirring up the hornet's nest of doom, to effect such changes. So again, we'll continue to argue for that. We'll continue to argue too for reviews of our state and local government public services and how we could do those differently and better. But they're kind of hedging around the edges. At the end of the day, our state is incredibly dependent on the distribution of GST. Again, I suppose fiddling with the way that that's actually determined, which, again, appears to be an effort of the bigger states to try and claw some money back to them, is very unhelpful for us.

20 **MS CHESTER:** You survived. Thank you very much for appearing. And we have covered a lot of ground with - - -

**MR BAILEY:** We have, and, again, I was sitting here listening and thinking we can tick that, we can tick that, we can tick that. But, again, I'll leave you my card and if you ever need any contact that would be absolutely fantastic.

25 **MS CHESTER:** We come down to Tassie quite often with many of our inquiries. So it's always good to have contacts with respective chambers. Thank you. On that note and before I do close our hearings here in Hobart, it would be remiss of me not to double-check that there's nobody else who's sneaked in who has a burning desire to share a view with us. If they'd like to, I'm happy to ask them to come up and join us. If not, I'm equally happy to call our Hobart hearings to a close, which is the end of all of our public hearings on HFE. Thank you one and all. We'll close the hearings.

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**ADJOURNED INDEFINITELY**

**[1.39 pm]**