



## WESTERN AUSTRALIAN FEDERAL PARLIAMENTARY LABOR PARTY

### SUBMISSION TO THE PRODUCTIVITY COMMISSION INQUIRY INTO HORIZONTAL FISCAL EQUALISATION

30 June 2017

#### *Introduction*

The Federal Government referred the issue of Horizontal Fiscal Equalisation (HFE) to the Productivity Commission for inquiry in April 2017. The referral has followed some years of public debate about the outcomes of the Commonwealth Grants Commission (CGC) process to distribute Goods and Services Tax (GST) revenue to the States and Territories.

The Western Australian Members of the Federal Parliamentary Labor Party (WAFPLP) jointly submit that the current GST relativity has produced negative outcomes for Western Australia that have profoundly impacted upon the ability of our State to respond to the immense challenges created by the current fiscal environment that it has inherited by an outgoing Liberal State Government.

The WA Treasury's pre-election financial projections statement revealed that the General Government Operating Deficit for 2016-17 now stands at \$3 billion, while total Public Sector Net Debt for the state is at over \$33 billion, and projected to reach up to \$41 billion within the forward estimates.<sup>1</sup> This compares with running surpluses over \$2 billion and a debt of \$3.6 billion at the height of WA's resources boom in 2008.<sup>2</sup>

The current disparity between Western Australia's contribution to the Commonwealth's GST receipts, as opposed to the return it receives, is inequitable and contrary to community expectation in Western Australia.

The incoming State Labor Government has inherited a dire economic outlook, with record levels of debt and deficit. It is clear that the Barnett Liberal Government wasted the resources construction boom in WA, failing to prepare for the inevitable decline in GST revenue and invest in the State for the next phase of growth required in a more diversified economy.

---

<sup>1</sup> WA Treasury, *2016-17 Pre-election Financial Projections Statement*, <http://static.treasury.wa.gov.au/2016-17-pfps/2016-17-pfps.pdf>, February 2017, p2.

<sup>2</sup> WA Treasury, *2007-08 Annual Report on State Finances*, [http://www.treasury.wa.gov.au/uploadedFiles/arsf\\_2008.pdf](http://www.treasury.wa.gov.au/uploadedFiles/arsf_2008.pdf), September 2008, p6.

Unless the inequity arising out of the current disparity in GST relativity (over a number of years) is urgently addressed, there is a real risk that despite being a resources powerhouse, Western Australia will not be able to contribute to the continued economic prosperity of our Nation.

This situation is not only avoidable, but it can (and should) be remedied by the Federal Government.

### ***Horizontal Fiscal Equalisation and the Commonwealth Grants Commission***

Horizontal Fiscal Equalisation has been a mainstay of Australia's Commonwealth-State relations since very early in the Federation's history. The principle of HFE is that to maintain economic and social cohesion between States, to maintain consistency in standards of government service provision to all Australians, and to ensure the stability of currency across jurisdictions with very different economies, States should share resources with each other.

Since its creation in 1933, the primary means of implementing the longstanding Federal Government commitment to HFE has been through the use of grants from the Commonwealth to the States according to a formula set out by the Commonwealth Grants Commission.

When the Federal Government adopted a Goods and Services Tax at the turn of this century, the revenue collected from the tax was provided directly back to State governments, according to a CGC formula. This was intended to:

- Replace various different State-based sales taxes, which were inconsistent between States and economically inefficient; and
- Address the vertical fiscal imbalance between the Commonwealth and the States by giving them a stable source of taxation revenue.

The formula is intended to take into account the respective revenue bases of States and Territories, as well as the varied costs between States of providing government services, such as health, education and infrastructure, given differing economic, geographical and resource realities.

### ***GST Relativity – A Western Australian Perspective***

The GST relativity refers to the relationship between actual distribution of GST revenue to States and Territories, compared to a hypothetical per-capita distribution. It is commonly expressed as a 'cents-in-the-dollar' figure.

Western Australia has felt the size and scale of the disparity of its GST relativity (as compared to other States and Territories) for some time.

In 2014-15 Western Australia's GST had the lowest relativity at 37.6 cents in the dollar, while the Northern Territory had the highest, receiving 566 cents in the dollar. That year, the next lowest relativity after Western Australia was Victoria, with a relativity of 88 cents in the dollar.

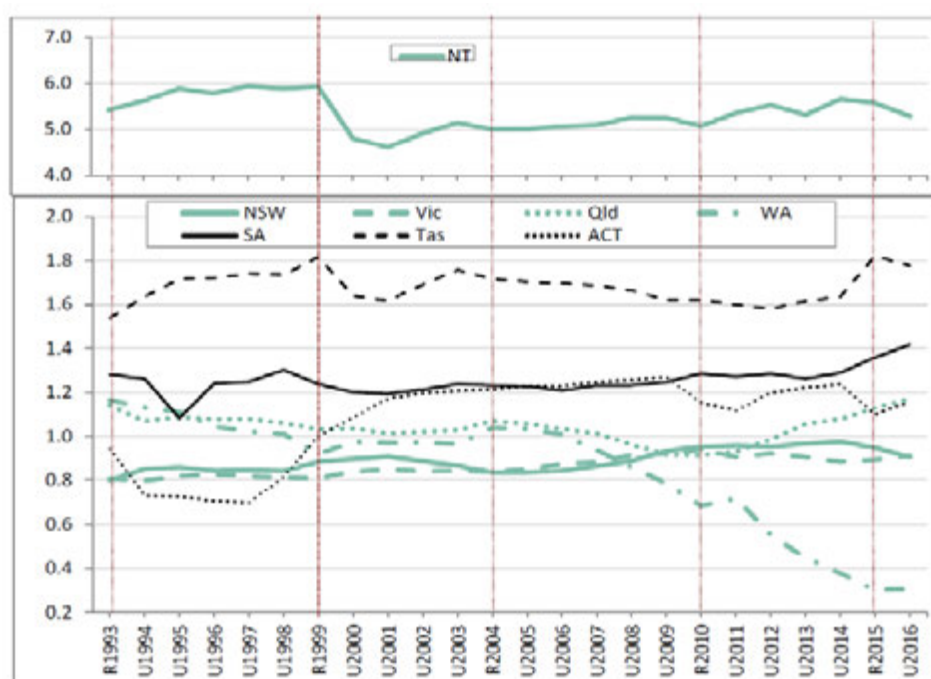
Western Australia's GST relativity for 2016-17 is 30.3 cents in the dollar.

In projections for the 2017-2018 financial year, Western Australia's GST relativity is 34.4 cents in the dollar.<sup>3</sup> Meanwhile the Northern Territory relativity is estimated at 466 cents of GST revenue in the dollar compared to a per-capita distribution, and the next lowest relativity after Western Australia will be New South Wales, with a relativity of 87.6 cents in the dollar (see table below).<sup>4</sup>

State or Territory	2017–18 relativity
NSW	0.87672
VIC	0.93239
QLD	1.18769
WA	0.34434
SA	1.43997
TAS	1.80477
ACT	1.19496
NT	4.66024

The graph below, from the Commonwealth Grants Commission, shows relativities for HFE since 1993.

**State per capita relativities, 1993 Review to 2016 Update<sup>5</sup>**



<sup>3</sup> Source: WA Government.

<sup>4</sup> Source: CGC 2017 Update Supporting Documentation Tables S9-2 and S9-3; Commonwealth Grants Commission, Tables S9-2 and S9-3, *2017 Update Supporting Documentation*: [https://www.cgc.gov.au/index.php?option=com\\_content&view=article&id=263&Itemid=542](https://www.cgc.gov.au/index.php?option=com_content&view=article&id=263&Itemid=542)

<sup>5</sup> Commonwealth Grants Commission, *Trends in Horizontal Fiscal Equalisation information paper CGC 2016-01*, April 2016, p2.

Note: The vertical lines indicate the years in which the Commission reviewed its assessment methods (for example, the 1999 Review). In the intervening years, the Commission updated the relativities using the same assessment methods as the preceding review. Source: *Commonwealth of Australia's Final Budget Outcome for 1993-94 to 2014-15* and Commission's *2016 Update Report on GST revenue sharing relativities*. Relativities from 1993-94 to 2008-09 were adjusted to be consistent with a pool comprising general revenue grants only.

The graph shows that, following a modest increase in 2003-04, WA's GST relativity has dropped sharply and remains stubbornly low in relation to other States, which is even more apparent since 2012.

Between 2011 and 2015, as WA's mining boom shifted from the construction to the production phase, there was a sharp decline in the State's revenue. Coupled with appalling financial management by the Barnett Government, deficits and a significant increase in net debt ensued, causing fiscal difficulties that continue to plague Western Australia's Treasury.

It should be noted that the CGC uses States' and Territories' budget outcome data rather than budget projections, and does so using a three-year rolling average. Because of this, the distribution can lag behind sudden changes in State revenues.

### ***Unintended disadvantage and the problems of disparity***

There are growing concerns around the economic and public policy problems that the low GST relativity in WA has the potential to cause over the medium to long term.

Much has been made of the harm HFE can cause to State competitiveness. Australia, however, does not have a pure HFE system, and so the empirical data that would support the 'disincentive' thesis is unclear. For example, at the aggregate level, States' own revenue streams as a proportion of their total revenue have been growing over time, though there remains a significant disparity in trends in own-source revenues in individual States (particularly those with high GST relativities).<sup>6</sup>

Some (in Western Australia in particular) have formed the view that the CGC's formula failed to take into account the social costs of rapid economic growth. During the height of the mining boom's construction phase prices of consumer goods and housing rose rapidly in Perth, creating some quite strange social and economic phenomena. This included increasing cost in the delivery of important social and community services as costs for labour rose. The inequality that resulted from that period of growth has meant that the subsequent economic downturn in Western Australia has also had a particularly stark social impact.

### ***GST Relativities and Remoteness***

There are also issues around changes made in 2015 to the CGC's formula for calculating remoteness. The CGC moved away from the 'SARIA' (State-based area remoteness index) to the ABS's ARIA (area remoteness index), meaning that the relative remoteness of a given locality is calculated from the closest population centre of over 250,000, rather than the State capital.

The change also saw a maximum 'remoteness' of 1,254km from a major population centre (ie: in WA's case, from Perth). However, the theory that there is no additional cost to provide State services further than 1,254km away from Perth bears no relationship to reality and only serves to impose an artificial cap on distributions to

---

<sup>6</sup> Commonwealth Grants Commission, 'Figure 1' and 'Figure 2', *Commonwealth State Financial Relations*, [https://www.cgc.gov.au/index.php?option=com\\_content&view=article&id=150&Itemid=316](https://www.cgc.gov.au/index.php?option=com_content&view=article&id=150&Itemid=316) pp6-7.

Western Australia. To be clear, the cap effectively deems Kununurra, Wyndham, Halls Creek, Broome, Derby, Eucla, Fitzroy Crossing, Karratha, Marble Bar, Port Hedland, Roebourne, Tom Price, Warburton and many other towns, some indeed in the order of 3,000kms away from Perth, as being as expensive to service as Exmouth.

This cap prevents adequate allocation of resources to provide for the very significant cost of servicing a State as geographically large and with a population as centralised as WA.

## ***Conclusion***

Federal Labor remains committed to the principles of Horizontal Fiscal Equalisation. It creates a consistent minimum standard of government services, economic conditions and standards of living across our nation. The WAFPLP seek an outcome to this situation, but one that doesn't negatively impact other States and Territories. Nevertheless, there is a growing chorus of disaffection with the current system of apportionment of GST revenue between States and Territories.

Western Australia, despite one of the largest mining booms in Australian history, has been left in a poor fiscal position by the outgoing Barnett Liberal Government. The most recent WA Government Budget updates demonstrate the extent of their financial negligence. This poor financial management is compounded by the additional injustice of the current GST distribution.

It is heartening to see the new McGowan Labor Government making rapid progress in restoring WA to economic strength, while ensuring a fair and secure society.

What is clear to the Western Australian community is the complete absence of any meaningful leadership from the Turnbull Government in this debate, in addressing the current level of disparity in Western Australia's allocation of GST revenue.

They have taken Western Australia for granted, colluded with the Barnett State Government for the last eight years, and failed to deliver a fair share for our State. Not nearly enough has been done to address the increasing inequity of GST distribution to Western Australia.

Western Australians – indeed citizens of other States too – quite rightly remain wary that any proposed long-term 'fix' by Malcolm Turnbull will involve increasing the rate of GST to 15 per cent.

The reality is that our local community is not particularly concerned by the specifics of formula adjustments or policy framework. They simply want the inequality fixed, so that confidence can be restored to our State's economy.

The WAFPLP welcomes the opportunity to make this submission to the Productivity Commission, and looks forward to reading the Commission's inquiry report in due course.

**TIM HAMMOND MP**

Shadow Minister for Consumer Affairs  
Shadow Minister Assisting for Resources  
Federal Member for Perth

**MATT KEOGH MP**

Federal Member for Burt

**ANNE ALY MP**

Federal Member for Cowan

**MADELEINE KING MP**

Federal Member for Brand

**JOSH WILSON MP**

Federal Member for Fremantle

**SENATOR SUE LINES**

Deputy President of the Senate and  
Temporary Chair of Committees  
Labor Senator For Western Australia

**SENATOR PAT DODSON**

Shadow Assistant Minister for Indigenous  
Affairs and Aboriginal and Torres Strait  
Islanders  
Labor Senator for Western Australia

**SENATOR LOUISE PRATT**

Shadow Assistant Minister for Families  
and Communities  
Labor Senator for Western Australia

**SENATOR GLENN STERLE**

Labor Senator for Western Australia