



**Response to
CGC Staff Discussion Paper
2008/19-S**

“New Issues for the 2009 Update”

Department of Treasury and Finance

September 2008

REFORM IN COMMONWEALTH-STATE FINANCIAL ARRANGEMENTS

The relativities for the 2009 Update will need to reflect the new Commonwealth-State financial arrangements in the assessment period.

Tasmania agrees that, until a final framework is agreed by COAG, it is not possible for the Commission to make any decisions regarding whether changes are required to the treatment of SPPs (or other, new types of payments) in its assessments. However, Tasmania notes that it is likely that SPPs will be distributed on an equal per capita basis in the future, and that the Commission will be instructed to treat Health Care Grants by inclusion, rather than by absorption.

TREATMENT OF NEW SPECIFIC PURPOSE PAYMENTS COMMENCED IN 2007-08

Tasmania has concerns about Commission staff's proposed treatment of some of the SPPs in Table 1. These concerns are discussed below for each payment.

Elective surgery waiting list reduction plan

Tasmania's understands that this particular payment is not an SPP and, in principle, should be treated by exclusion.

While National Partnerships are yet to come into existence as a type of Commonwealth payment to the states (this will occur from 1 January 2009), a number of payments have been notionally attributed to a National Partnership in readiness for the commencement date. For example, Commonwealth Budget Paper No. 3 identifies the waiting list reduction plan as a National Partnership payment.¹ Of the two types of National Partnerships (project and reform), the plan is clearly a reform NP, as it involves both facilitation and reward payments.

Although the CGC treatment of NP agreements has not been finalised, COAG agreed on 26 March 2008 that reform NPs should generally be excluded from the CGC process.² The rationale is that an exclusion treatment ensures that 'any benefit to a state from achieving specified outputs sought by the Commonwealth, or through implementing reforms, would not be redistributed to other states through the equalisation process'. Tasmania interprets this as meaning that the CGC should automatically treat reform NPs by exclusion and should not normally consider their treatment unless directed to.

Further work being developed to go to COAG on 2 October 2008 is consistent with the previous COAG decision in March 2008.

¹ Commonwealth Budget Paper No. 3 2008-09, pages 37-38.

² *Reform of Specific Purpose Payment (SPP) Arrangements*, Ministerial Council Report to COAG, 14 March 2008.

Helping public patients in hospitals for nursing home places

Tasmania agrees that this payment has a direct impact on State budgets and, in principle, supports its inclusion treatment. However, we note that this payment is also listed in Commonwealth Budget papers as a National Partnership, although it is unclear whether it is regarded as a reform or project payment. We recommend that the Commission seek advice from the Australian Treasury as to whether this payment is a reform or project payment, as this may affect its treatment.

Family Violence Partnership

It is not clear to Tasmania why this payment should be treated by exclusion.

Although the Discussion Paper refers to this payment as 'reimbursement', funding for this program supports the reduction of family violence, which would normally be regarded as a state service (falling under law and order, health and/or community services). Expense differences are assessed for these services and the impact of indigenous over-representation is included in these assessments. Tasmania would have expected that the family violence partnership payment reduces what states would otherwise have to spend on these services.

This partnership was previously a COPE, but this should not determine its treatment now. Its impact on state budgets should determine its treatment. Tasmania recommends that the Commission reconsider whether there are grounds for excluding this payment.

NORTHERN TERRITORY EMERGENCY RESPONSE (NTER)

Assuming the 2009 Update Terms of Reference are the same as for the 2008 Update, Tasmania accepts the Commission Staff proposal to exclude any Australian Government payments relating to the NTER from the Northern Territory's revenue and exclude the expenses funded by the Australian Government payment for NTER from the Northern Territory's expenses.

Tasmania considers that the NTER could result in some additional costs in providing services to Indigenous people and some cost savings for the Northern Territory Government. Tasmania accepts the Commission is not in a position to collect information to quantify the net impact.

MERSEY HOSPITAL IN TASMANIA

Assuming that the 2009 Update Terms of Reference will again require that "the Mersey Hospital arrangements have no impact on the distribution of GST and Health Care Grants", the Commission staff propose to recommend that:

- any Australian Government payments or expenses relating to the Mersey Hospital be excluded from Tasmania's revenue;
- expenses incurred by the Australian Government be added back to Tasmania's Inpatient expenses; and

- Mersey Hospital inpatient separations be reflected in the public hospital use figures.

Tasmania endorses the staff's recommended approach as satisfying the ToR instruction. That is, the effect of these actions will be to restore, for the purposes of the Commission's assessments, the status quo prior to the Commonwealth take-over (ie. the Mersey Hospital as a public hospital within the Tasmanian public hospital system).

PAYROLL TAX AND ABS PUBLIC SECTOR WAGES AND SALARIES DATA

Tasmania does not oppose the Commission staff proposal to use the trend increase in public sector earnings over the previous five years to increase the 2006-07 public sector earnings data to make an estimate for 2007-08, should actual data not be available in time for the 2009 Update.

Tasmania's own analysis over a longer time period confirms that the use of a trend estimate has historically produced an outcome close to the actual outcome. However, there are points in time when a change in trend can be detected and this highlights the risk in using recent outcomes as a predictor of future outcomes. In this context, the proposed approach does not guarantee that the estimate will be close to the actual outcome for 2007-08 data. Notwithstanding this concern, Tasmania does not have an alternative to suggest.

While it is not discussed in the Staff Discussion paper, Tasmania understands that Commission staff have analysed and confirmed that the observed small differences between actual and estimated data (eg less than 3 per cent) translates into an immaterial impact on the redistribution between states.

UPDATING WAGE INPUT COSTS

Tasmania opposes the Commission staff proposal to recommend that the changes in states' wage cost indexes (WCI) be used to update the 2005-06 SET based relativities for the 2006-07 and 2007-08 assessment years.

While Tasmania is aware that this labour price index approach is under consideration within the context of the 2010 Review location assessment, Tasmania is strongly of the view that it would be premature to introduce it for the 2009 Update. It constitutes a significant change of method which appears to be "still in development", has not been exposed to state scrutiny/debate but which could be expected to have material distributional consequences.

As the New Developments Paper acknowledges, the WCI is based on states' individual economic structures, rather than a national economic structure (the wage cost differential measurement base under the SET approach). This gives rise to WCI wage differential measures which, to some greater or lesser degree, reflect state differences in industrial and occupational mix, inconsistent with the 2004 Review SET base. Paragraph 35 states that the impact of these structural differences on the actual data "appear to be much

less than the measurement errors associated with the assessment”, and that “the impact of industrial structure is generally greater in smaller states”. Neither of these observations is particularly reassuring. Paragraph 36 suggests that these structural differences could be dealt with through specific adjustment or discounting if deemed necessary (but without further details).

The limited, high level analytical detail contained in the New Developments Paper is insufficient to allow a proper evaluation of how well a WCI updating method would “mesh” with the SET (base) method but does suggest some unresolved measurement concerns. Within this context, the introduction of a WCI approach in the last year of the 2004 Review period appears to pre-empt a more detailed and considered examination of the proposal within the 2010 Review.

In lieu of New Developments Paper’s proposal, Tasmania supports the extension of the 2008 Update decisions for the assessment year 2006-07 to the 2009 Update assessment years 2006-07 and 2007-08.

Tasmania notes that there has been no change of circumstances for the 2009 Update such as to justify a departure from the Commission’s previous Tasmanian SET adjustment judgement.

The SET results do not provide a realistic result for Tasmania. The Commission acknowledged a case for this due to Tasmania’s structural peculiarities at the outset of the 2004 Review and used its judgement to adjust the SET modelled outcomes for Tasmania. This judgement was subsequently re-affirmed for the SET 2005 modelling, resulting in Tasmania’s modelled outcome being once again adjusted.

Regardless of the decision that the Commission now makes for the 2009 Update (whether to repeat the 2008 Update approach or to update the SET 2005-06 base using the WCI-based approach), the 2005 SET base used for Tasmania should remain the judgement-adjusted base, not the modelled outcome base.

ABOLITION OF STAMP DUTY ON NON-REAL BUSINESS TRANSACTIONS IN THE ACT

Tasmania agrees that there is a case to introduce an adjustment to ACT’s revenue base from 2007-08 to account for its decision to abolish duty on non-residential conveyances other than real property transactions. The analysis to justify a 1 per cent adjustment appears reasonable.

ADDITIONAL ISSUE RAISED BY TASMANIA – ADJUSTMENT TO TASMANIA’S CONVEYANCE DUTY BASE FOR CORPORATE RECONSTRUCTIONS

Tasmania is of the understanding that it is the only state in which corporate reconstructions are not exempt from duty. Because of this, Tasmania is unable to identify and separate out corporate reconstructions from the data that is provided in the Update. This has the effect of increasing Tasmania’s

assessed tax base, and therefore its assessed revenue raising capacity, above what it should be.

Tasmania acknowledges that the lack of data available to estimate how much Tasmania's tax base should be adjusted down is a challenge. However, corporate reconstructions occur on a regular basis within Tasmania, as they do in other states. Tasmania has very limited data, generally around large transactions in which *ex-gratia* assistance is sought. These are not particularly useful, however, in understanding the overall level of corporate reconstruction activity in a given year.

In this context, Tasmania suggests a conservative, judgement-based adjustment would be appropriate. One option would be to take the state with the lowest proportion of corporate reconstructions out of its total duty transactions, and apply that proportion to Tasmania's tax base to determine the adjustment. The adjustment would need to be made to each year of the assessment period.