



# **COMMONWEALTH GRANTS COMMISSION**

**DRAFT ASSESSMENT PAPER CGC 2003/71**

## **NATIONAL CAPITAL FACTORS**

Prepared for the Commission's 2003 Conferences on Draft Assessments

**AUGUST 2003**

## NOTE

**Included in this paper are the results of preliminary calculations based on the methods proposed throughout the paper and using the data currently available. Those results are indicative only and should be seen as work in progress. Ongoing changes are being made to standards and factor calculations as new data come to hand. Moreover, the calculations have been done using a prototype assessment system and are subject to ongoing revision as checking processes proceed.**

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## INTRODUCTION

1. The terms of reference for the 2004 Review ask the Commission to:  
  
‘... review whether the allowances for special circumstances granted to the Australian Capital Territory continue to be necessary and, if so, make appropriate allowances.’
2. National capital allowances make provision for one type of special circumstances. They have been a feature of the Commission’s assessments of ACT finances since 1984.
3. This paper reviews conceptual issues related to the assessment of national capital factors and sets out assessment guidelines. Category-specific national capital issues are considered in the relevant draft assessment papers.

## THE 1999 REVIEW ASSESSMENT

### *Description of allowances assessed*

4. In the 1999 Review, the national capital factor made allowance for cost influences that arise because of Canberra’s status as the national capital and the seat of government. These influences, unique to the ACT, cause increases in the cost of providing normal State-type services in the ACT.
5. Funding for national capital allowances is provided from the GST revenue pool.

### *Importance of current assessment*

6. In the 2003 Update, the Commission assessed national capital factors in a number of categories. Table 1 shows the amount assessed for each category in the 1999 Review.

**Table 1** NATIONAL CAPITAL FACTOR ALLOWANCES, 1999 REVIEW

Category	1999 Review assessed allowances
	\$m
Education	4.000
General Public Services (Regulatory and Other Services)	3.400
Administration of Justice	0.200
Culture and Recreation	1.385
Urban Transit	1.500
Public Safety and Emergency Services	0.615
<b>Total allowance</b>	<b>11.100</b>

Source: 1999 Review Working Papers.

## CONCEPTUAL ISSUES

7. The conceptual issues related to the assessment of national capital factors for the 2004 Review concern the case for their continued assessment, and whether they should be funded from GST revenue.

8. **Preliminary State views.** In its main submission, the ACT proposed new allowances for Housing, Roads, Tourism, Primary Industry, and National Parks and Wildlife Services that totalled approximately \$24 million. These new allowances, in addition to the increases in allowances across existing categories, brought the total national capital allowances sought to \$48.8 million.

9. **Staff proposals.** In *Discussion Paper CGC 2002/05, Cross-border Disabilities and Special Circumstances of the Australian Capital Territory*, the States and the Commonwealth were invited to comment on whether disabilities due to national capital influences should be assessed in the current manner, or whether they should be phased out or removed from the equalisation process, with a view to the fiscal responsibility being transferred to the Commonwealth.

10. In the annotated agenda for the planned staff level conference on ACT Special Circumstances (scheduled for 6 February 2003 but subsequently cancelled due to the impact of the Canberra bushfires), States were provided with a further opportunity to respond to questions regarding the national capital issues.

11. **Further State views.** The ACT argued for a continuation of national capital allowances because the financial impact on the ACT resulting from its role as the national capital and seat of government was significant and was underestimated by current assessments.

12. The ACT revised the level of the allowances sought for the 2004 Review to almost \$75 million, up from \$11.1 million assessed in the 1999 Review. The revised

allowances were underpinned by new accounting methods and improved data. The ACT provided much evidence in its submissions and workplace presentations regarding the financial impact of national capital influences.

13. The ACT argued that the assessment of national capital cost influences should not be time-limited. It contended that many of its allowances reflected current cost impositions and related to recent (and new) or ongoing Commonwealth decisions and not just cost legacies. It argued that the impacts were not reducing.

14. Regarding the funding mechanism for national capital allowances, the ACT said that national capital obligations were a responsibility of the Australian community and the costs of national capital administration and maintenance should be shared among the Australian community. However, it acknowledged that such an arrangement was inconsistent with national tax reform because all GST belongs to the States. Within that framework, the ACT noted that some parties had argued that the States were funding Commonwealth responsibilities.

15. The ACT therefore proposed a classification system where responsibilities for national capital allowances were identified and shared by the States (funded inside the GST revenue pool) and the Commonwealth (funded outside the GST revenue pool).

16. In its submission for the 2004 Review, the Australian Treasury said that the Commission's horizontal fiscal equalisation mandate points toward its continued assessment of all relevant factors affecting the demand for and cost of State-like services — including any that can reasonably be attributed to national capital influences.

17. The National Capital Authority has acknowledged that the ACT faces additional costs in the delivery of a number of State-type services due to it being the national capital and the seat of government.

18. No other States commented.

19. **Commission decision.** There is little disagreement with the underlying proposition that ACT faces some additional costs in the delivery of some State-type services because it is the national capital and the seat of government. The Commission considers that the conceptual case for the assessment of national capital allowances is sound.

20. The various conceptual arguments suggest that national capital and other allowances for the special circumstances of the ACT should be tightly defined and that the other States should not bear the costs of Commonwealth responsibilities. The Commission has decided that it will continue to assess allowances for the special circumstances of the ACT subject to the following principles:

- (i) Assessments should be made under equalisation principles for additional costs incurred by the ACT that are undeniably the result of mandated influences that arise because of Canberra's status as the national capital and the seat of government. Those assessments would be described as national capital allowances. The individual merit of each proposed allowance would be examined.

- (ii) Commonwealth cost legacies inherited by the ACT after self-government would be assessed as special fiscal needs allowances. Equalisation would not apply to these items (that is, any allowances assessed should be paid outside the GST pool arrangements). Special fiscal needs allowances should be phased out over an appropriate number of years.
- (iii) Where Commonwealth policy influences are having an effect on any State, and it is standard policy for bilateral arrangements to be made, then no assessment should be made. Such arrangements would be out of scope (such as the Commonwealth Fire Brigade arrangements).
- (iv) Where Commonwealth policy influences are having an effect on any State, and it is not standard policy for bilateral arrangements to be made, and a case can be made for a factor, then an assessment should be made from within the pool (for example, Land Rights, Native Title, Superannuation).

21. Subject to those principles, the Commission will continue to assess national capital allowances when it is convinced they are justified by the circumstances surrounding specific services.

## **ASSESSMENT APPROACH**

22. The ACT's proposals for national capital allowances in specific categories have been considered in the relevant draft assessment papers (and in accordance with the assessment guidelines set out in *Draft Assessment Paper CGC 2003/12, Assessment Guidelines*). In doing so, the 1999 Review assessments formed the starting point for analysis of new ACT proposed allowances.

23. In addition to the general assessment guidelines, the following checks have been applied to the assessment of national capital allowances:

- (i) Is the cost an unavoidable impact of the National Capital Plan or Commonwealth policy (legacy) relating to the national capital? An assessment should be made if it is and the cost is not within the control of the ACT government.
- (ii) Is the cost likely to be incurred by other States? An assessment should only be made if the national capital influence results in above-standard costs not incurred by other States.
- (iii) Does the cost relate to a State or municipal activity? No assessment should be made in relation to a municipal activity. The ACT's municipal costs are met through a separate SPP.

24. Category-specific national capital allowances have been considered in the relevant draft assessment papers.

25. Table 2 sets out the allowances proposed by the ACT in its 2004 Review Rejoinder Submission. It also summarises the allowances the Commission currently proposes to assess in the 2004 Review.

26. Table A-1 in the attachment provides an overview of national capital allowances assessed for the 1999 Review and the 2004 Review, using the assessment guidelines and methods.

**Table 2** NATIONAL CAPITAL ALLOWANCES, ALLOWANCES SOUGHT AND PROPOSED ALLOWANCES, 2004 REVIEW DRAFT ASSESSMENT

Category	2004 Review allowance sought	2004 Review proposed allowance
	\$m	\$m
Education	4.000	0.000
General Public Services	33.387	2.500
Culture and Recreation	5.800	1.000
Urban Transit	2.100	0.500
Public Safety and Emergency Services	3.300	0.900
Housing	13.000	0.000
National Parks and Wildlife Services	0.500	0.100
Roads	6.400	0.000
Tourism	5.700	0.000
Primary Industry	0.572	0.000
<b>Total allowances</b>	<b>74.759</b>	<b>5.000</b>

Source: ACT Rejoinder Submission to the 2004 Review and Commonwealth Grants Commission decisions.

27. A component weight for each category in which an allowance is assessed will be calculated by dividing the assessed allowance by the Australian standard expense for the category, to give the proportion of total standard expense to which the factor is applied.

28. Factors will be calculated by dividing the Australian mean resident population by the ACT mean resident population. This approach is called the general method in Table A-1.

**Table A-1 NATIONAL CAPITAL ALLOWANCES, 1999 REVIEW ASSESSMENT AND 2004 REVIEW DRAFT ASSESSMENT**

Category	1999 Review	2004 Review	Changes	Basis of calculation
Education	<p>The factor accounted for the extra costs associated with teaching English to children of diplomats. Because the ACT had a disproportionate number of diplomatic children relative to other States, the assessment reflected the additional costs of diplomatic students in the ACT.</p>	<p>A factor has not been assessed because the updated amount of the allowance was not material.</p>		
General Public Services	<p>In the 2003 Update, an amount of \$3.4 million was assessed to allow for:</p> <ul style="list-style-type: none"> <li>- Extra capital costs imposed by siting and building requirements of the national capital plan, and additional requirements in relation to infrastructure provisions (\$1 million).</li> <li>- The leasehold system increased the costs of planning and management (\$2 million).</li> <li>- Increased costs of planning functions because the ACT had to consider issues associated with the integration of its services with those provided in contiguous areas in New South Wales (\$0.4 million).</li> </ul>	<p>The Commission has estimated a national capital allowance of \$2.5 million made up of: capital works (\$1 million); and planning and development (\$1.5 million).</p>	<p>A conceptual case was not made that extra costs associated with strategic regional planning arose because of mandated influences arising from the ACT's status as the national capital. Evidence was not provided to support the case that extra costs are associated with the leasehold system relative to land tenure systems in the States or that extra net costs were incurred arising from foregone opportunities for land development.</p>	<p>The general method was applied.</p>

**Table A-1 NATIONAL CAPITAL ALLOWANCES, 1999 REVIEW ASSESSMENT AND 2004 REVIEW DRAFT ASSESSMENT (continued)**

Category	1999 Review	2004 Review	Changes	Basis of calculation
Administration of Justice	An amount of \$0.2 million was assessed to allow for criminal injuries compensation claims arising out of Commonwealth matters.	A factor has not been assessed, because the ACT has introduced new criminal compensation legislation which removed the justification for the assessment.	The Commission removed this assessment for the 2004 Review.	
Culture and Recreation	This factor allowed for the above standard level of open space and sportsgrounds in Canberra. An allowance of \$4.50 per capita (\$1.39 million) was assessed.	An allowance of \$1 million has been assessed to allow for the additional costs incurred in maintaining Commonwealth Designated Land Areas in the ACT. No allowances have been assessed for: (i) above standard width of road verges, or above standard area of sportsgrounds and urban open space; and (ii) above average costs of maintaining this above average width of road verges.	The allowance assessed is based on the additional costs of maintaining Commonwealth Designated Land Areas in the ACT, and not the above average level of open space and sportsgrounds in the ACT.	The general method was applied.
Urban Transit	This factor allowed for the effect of Commonwealth policies on pay parking on bus patronage. An annual allowance of \$1.5 million was assessed, based on an estimate of reduced fare revenue arising from the Commonwealth policy of not imposing parking fees in the Parliamentary Triangle.	An annual allowance of \$0.5 million was proposed, based on an estimate of parking spaces in the parliamentary triangle, over which the Commonwealth has direct control and the propensity for people to use public transport for journeys to work.	The allowance was calculated by multiplying the number of Commonwealth parking spaces by average car occupancy, by average bus use ratio, by the number of working days and by a return fare of \$4 a day.	The general method was applied.

**Table A-1 NATIONAL CAPITAL ALLOWANCES, 1999 REVIEW ASSESSMENT AND 2004 REVIEW DRAFT ASSESSMENT (continued)**

Category	1999 Review	2004 Review	Changes	Basis of calculation
Public Safety	An amount of \$2 per capita (\$615 000) was assessed to allow for: (i) the additional costs of employing bush fire fighters rather than volunteers; and (ii) the extent of the bush – urban interface and open space in and around the city.	An allowance of \$900 000 has been assessed to allow for: (i) the extent of the bush – urban interface and open space in and around the city (\$500 000); and (ii) the increased costs arising from the threat of terrorism (400 000).	An allowance has not been assessed for volunteer fire-fighters because the conceptual case was not made that it is a mandated influence arising from the ACT’s status as the national capital. However, a case was made that extra costs arising from the heightened risk of terrorism was a mandated influence arising from the ACT’s status as the national capital.	The general method was applied.
Housing	Not assessed in the 1999 Review.	Not assessed in the 2004 Review. The ACT has not established a conceptual case that its situation results from a mandated influence arising from its status as the national capital.  It was not clear that the ACT’s position was materially different from that of other States, except that, before self-government, the Commonwealth managed the stock.  There may have been a backlog of unfunded maintenance in the stock the ACT inherited and the stock may not necessarily match requirements.		

**Table A-1 NATIONAL CAPITAL ALLOWANCES, 1999 REVIEW ASSESSMENT AND 2004 REVIEW DRAFT ASSESSMENT (continued)**

Category	1999 Review	2004 Review	Changes	Basis of calculation
National Parks and Wildlife Services	Not assessed in the 1999 Review.	<p>But all States face similar situations. Because the ACT had a large stock it may have had greater flexibility in managing it.</p> <p>An allowance of \$100 000 has been assessed to allow for the additional costs incurred by the ACT in producing a management plan for the Canberra Nature Park arising from extra consultation time and need for works approvals.</p>		The general method was applied.
Roads	Not assessed in the 1999 Review.	<p>A factor has not been assessed, because a conceptual case was not been made that any above-standard width of arterial roads in the ACT or shorter life span was a mandated influence of the ACT's status as the national capital.</p>		
Tourism	Not assessed in the 1999 Review.	<p>A factor has not been assessed, because a conceptual case was not been made that the costs arose from a mandated influence arising from the ACT's status as the national capital. Also the Commission regards expenditure by the Canberra Tourism and Events Corporation to be economic development, which is more appropriately assessed by the equal per capita method.</p>		

**Table A-1 NATIONAL CAPITAL ALLOWANCES, 1999 REVIEW ASSESSMENT AND 2004 REVIEW DRAFT ASSESSMENT (continued)**

Category	1999 Review	2004 Review	Changes	Basis of calculation
Primary Industry	Not assessed in the 1999 Review.	No allowance will be assessed because a conceptual case was not been made that the costs arose from a mandated influence arising from the ACT's status as the national capital. Also the Commission considered the net impact of forestry operations was an economic development-type expense, which it has assessed by the equal per capita method.		