Australian Government

Commonwealth Grants Commission

Report on
GST Revenue Sharing Relativities

2018 Update

Canberra

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A copy of this report can be obtained from the Commission's website (https://cgc.gov.au/).

LETTER OF TRANSMITTAL

Australian Government

Commonwealth Grants Commission

LETTER OF TRANSMITTAL

28 March 2018

The Hon Scott Morrison MP
Treasurer
Parliament House
CANBERRA ACT 2600

Dear Treasurer

As members of the Commonwealth Grants Commission appointed under the *Commonwealth Grants Commission Act 1973*, and in response to the terms of reference provided by you on 27 March 2018, we have prepared this report to provide updated per capita relativities for use in distributing GST revenue among the States and Territories in 2018-19.

In accordance with those terms of reference, we are also providing the results of the update to the States and Territories today.

Yours sincerely

G J Smith
Chairperson

J D Petchey
Member

L S Williams AM
Member

P W Hendy
Member

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ACKNOWLEDGEMENTS

The Commission appreciates the ready co-operation extended to it and its staff during this update by staff of Commonwealth and State Treasuries and other agencies.

The Commission also acknowledges the commitment and capable contribution of its staff.

TERMS OF REFERENCE

TREASURER

Mr Greg Smith
Chairperson
Commonwealth Grants Commission
Second floor, Phoenix House
86-88 Northbourne Ave
BRADDON ACT 2612

Dear Mr Smith

I am writing to you to convey the enclosed terms of reference for the Commonwealth Grants Commission's *2018 Update of GST Revenue Sharing Relativities* (2018 Update). I apologise for the delay in providing them to you.

The Commission should provide its report to the Government by 28 March 2018. A copy of the report should also be provided, under embargo, to the States and Territories by 28 March 2018. I anticipate making the report publicly available following a short embargo period.

Yours sincerely

The Hon Scott Morrison MP
26 / 3 / 2018

Parliament House Canberra ACT 2600 Australia
Telephone: 61 2 6277 7340 | Facsimile: 61 2 6273 3420

Terms of Reference for the 2018 Update of GST Revenue Sharing Relativities

COMMONWEALTH GRANTS COMMISSION ACT 1973

I, Scott John Morrison, Treasurer, pursuant to sections 16, 16A and 16AA of the *Commonwealth Grants Commission Act 1973*, refer to the Commission for inquiry into and report upon the recommended per capita relativities to be used to distribute GST revenue among the States, the Northern Territory and the Australian Capital Territory (collectively referred to as the States) in 2018-19. The Commission should provide a copy of its report, under embargo, to the Commonwealth and the State Treasuries by 28 March 2018.

2. The Commission should undertake an assessment of the per capita relativities recommended to be used to distribute GST revenue among the States in 2018-19 (the GST relativities).

3. The Commission's assessment should take into account the *Intergovernmental Agreement on Federal Financial Relations* (as amended), which provides that GST revenue will be distributed among the States in accordance with the principle of horizontal fiscal equalisation.

4. The Commission's assessment should be based on the review period 2014-15 to 2016-17 inclusive. Where possible, the Commission should use the latest available data.

5. Subject to paragraphs 6 – 8, the Commission's assessment should be based on the application of the same principles, categories and methods of assessment that the Commission used to calculate the per capita relativities in its *Report on GST Revenue Sharing Relativities – 2017 Update*.

6. The Commission's assessment should treat Commonwealth payments to the States as follows:

   (a) National Specific Purpose Payments (NSPPs), National Health Reform (NHR) funding, Quality Schools funding (for government schools) and National Partnership project payments should affect the relativities, recognising that these payments provide the States with budget support for providing standard state services.

      i. NHR funding and corresponding expenditure relating to the provision of cross-border services to the residents of other States should be allocated to States on the basis of residence.

   (b) National Partnership facilitation and reward payments should not affect the relativities, so that any benefit to a State from achieving specified outputs sought by the Commonwealth, or through implementing reforms, will not be redistributed to other States through the horizontal fiscal equalisation process.

   (c) General revenue assistance, excluding GST payments, will affect the relativities, recognising that these payments are available to provide untied general budget support to a State.

(d) Notwithstanding subparagraphs 6(a) – (c), the Commission may determine that it is appropriate for particular payments to be treated differently, reflecting the nature of the particular payment and the role of State governments in providing particular services.

(e) Those payments which the Commission has previously been directed to treat as having no direct influence on the relativities, including payments for which the Commission has been directed to apply a 50 per cent discount, should continue to be treated in that way. Where those payments are replaced, the treatment of the new payment should be guided by subparagraphs 6(a) – (d), unless otherwise directed.

7. The Commission should prepare its assessment on a basis consistent with the Commonwealth's intention that the following Commonwealth payments should not directly influence the per capita relativities:

(a) $730.4 million to Tasmania relating to the transfer of ownership of the Mersey Community Hospital;

(b) $1.42 billion to Victoria relating to the Regional Rail Revival program; and

(c) $1.2 billion to Western Australia relating to the re-allocated Perth Freight Link infrastructure funding.

8. If data problems necessitate changes, the Commission should proceed on the basis that:

(a) new, more reliable data would be used in the first possible update, if method changes were not required; or

(b) if overcoming the data problems necessitated method changes, revised methods would be used in the first possible update, subject to consultation with the States during that update.

9. The Commission should consult the Commonwealth and the States before deciding on any changes in methods that arise as a result of a significant change in arrangements which govern Commonwealth-State relations and which are considered appropriate for the Commission to fulfil its obligations in respect of these terms of reference.

10. To the extent possible, the Commission should, upon reporting, provide all parties with details underpinning its calculations and assessments, and endeavour to meet requests for supplementary calculations.

SCOTT JOHN MORRISON

THE TASK

This report contains the Commission's response to the terms of reference for the 2018 Update received from the Commonwealth Treasurer on 27 March 2018.

The Commission has been asked to advise how Goods and Services Tax (GST) revenue should be distributed among the States in 2018-19. As directed in the terms of reference the Commission has:

- used the same principles and methods used in the 2017 Update
- used the latest available reliable data for the three years 2014-15 to 2016-17
- followed the guidance on the treatment of Commonwealth payments and direction on how some payments should be treated.

Details of the Commission's task are in Chapter 1 of the *Report on GST Revenue Sharing Relativities, 2015 Review, Volume 1* and the principles used in undertaking it are in Chapter 1 of Volume 2 in the same report. These documents are available on the Commission's website (https://cgc.gov.au/). An overview of the Commission's update processes is also available on the website.

CONTENTS

OVERVIEW

EXECUTIVE SUMMARY

This report recommends a distribution of GST revenue among the States in 2018-19 designed to give each of them the fiscal capacity to deliver services and the associated infrastructure at the same (average) standard, if each made the average effort to raise revenue from its own sources and operated at the average level of efficiency.

The GST distribution is based on the same methods applied in the 2017 Update, but using updated data, as required by the Commission's terms of reference. It incorporates 2016-17 data for the first time while, under the three-year averaging process, 2013-14 data drop out. Data associated with the 2016 Census are also incorporated for the first time.

While Western Australia remains the fiscally strongest State, its fiscal advantages have declined, leading to an increase in its GST share. Between 2013-14 and 2016-17, the value of iron ore production fell, while the value of coal production increased. This reduced the fiscal capacity of Western Australia, while increasing that of New South Wales and Queensland. Western Australia has also had below average growth in property sales and taxable payrolls. These impacts on Western Australia's revenue capacity were partly offset by a decline in its share of national population growth, which reduced its need for investment spending.

The assessed fiscal capacities of New South Wales, Queensland, Tasmania, the ACT and the Northern Territory have increased, reducing those States' GST shares. Strong growth in property markets and taxable payrolls increased the fiscal capacity of New South Wales. In addition to the effects of mining developments, Queensland's GST share fell as its earlier natural disaster spending needs have largely passed. The improvement in the fiscal capacity of Tasmania was driven by an increase in its revenue raising capacity and in its share of Commonwealth payments. The ACT's stronger fiscal capacity resulted from above average growth in property sales and taxable payrolls. The stronger fiscal capacity of the Northern Territory resulted from a fall in its relative service delivery costs and investment requirements, as well as an increase in its share of Commonwealth payments.

The assessed fiscal capacities of the other two States have fallen, increasing those States' GST shares. Victoria's increased GST share is largely due to a fall in its share of Commonwealth payments and an increase in its investment requirements stemming from a greater share of national population growth. These trends more than offset its stronger payroll and property tax bases. South Australia's weaker relative fiscal capacity reflects slow growth in its tax bases.

The size of the redistribution of GST revenue away from equal per capita (EPC) to the States with below average fiscal capacities again fell in this update from $7.8 billion to $6.8 billion.

RECOMMENDED GST DISTRIBUTION

1 Table 1 shows the per capita relativities the Commission recommends for use in distributing the GST revenue among the States in 2018-19. It also shows State shares of the GST revenue implied by the Commission's 2018-19 recommendations and an illustrative GST revenue distribution. It compares these with the results for 2017-18.

Table 1 Relativities, shares and illustrative GST distribution, 2017-18 and 2018-19

	Relativities		GST shares		GST distribution	
	2017-18	2018-19	2017-18	2018-19	2017-18	2018-19
			%	%	$m	$m
New South Wales	0.87672	0.85517	28.1	27.4	17 511	18 030
Victoria	0.93239	0.98670	24.0	25.6	14 989	16 830
Queensland	1.18769	1.09584	23.8	22.0	14 848	14 447
Western Australia	0.34434	0.47287	3.6	4.9	2 255	3 255
South Australia	1.43997	1.47727	10.1	10.3	6 284	6 751
Tasmania	1.80477	1.76706	3.8	3.7	2 378	2 434
Australian Capital Territory	1.19496	1.18070	2.0	2.0	1 244	1 298
Northern Territory	4.66024	4.25816	4.6	4.2	2 891	2 755
Total	1.00000	1.00000	100.0	100.0	62 400	65 800

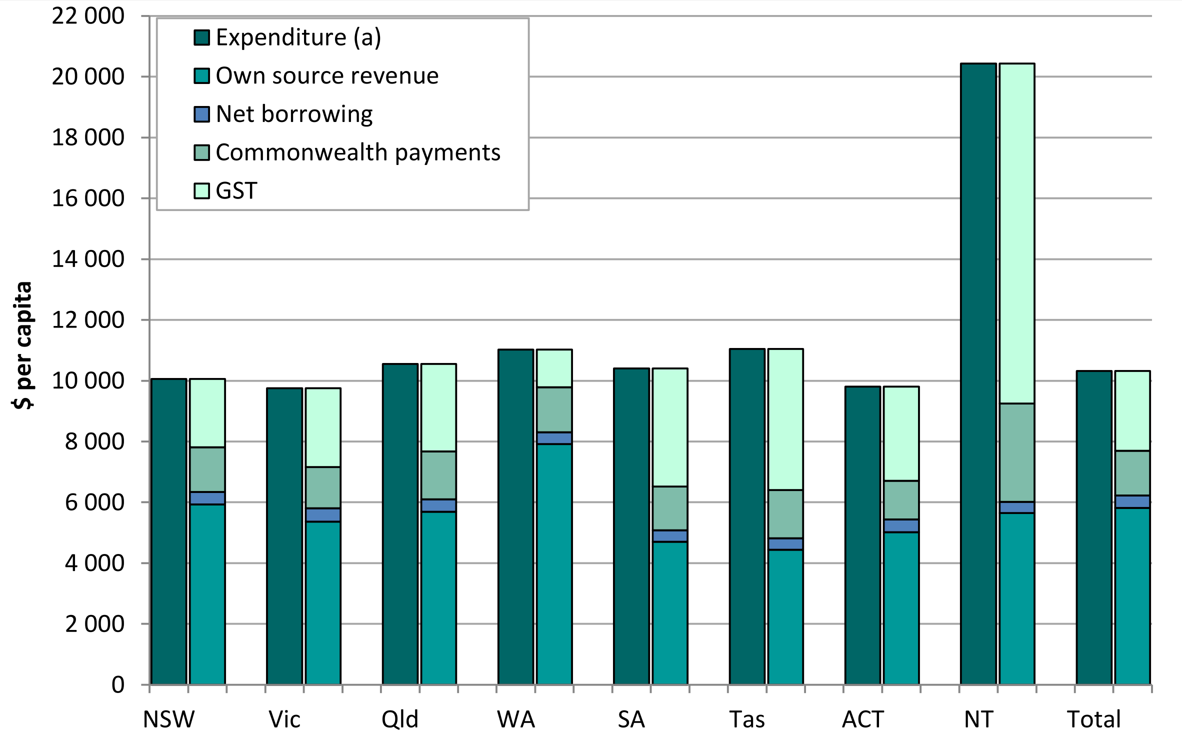
Source: Commission calculation.

2 The methods used to derive these results for 2018-19 are set out in the *Report on GST Revenue Sharing Relativities, 2015 Review* and the *Report on GST Revenue Sharing Relativities, 2017 Update*. Using these methods, and data for 2014-15, 2015-16 and 2016-17, the Commission has measured how the economic, social, demographic and other characteristics of the States affect the relative expenses States need to incur to provide services (including infrastructure) and the relative capacity of States to raise their own revenue. The expense and revenue assessments are then combined with the additional Commonwealth support States receive and State populations, to calculate State shares of the GST.[1] These shares aim to give each State in 2018-19 the fiscal capacity to provide the average standard of services and associated infrastructure for its population, if it makes the average effort to raise revenue and operates at the average level of efficiency.

3 Figure 1 illustrates the outcomes of this process. It shows that the per capita GST requirement for each State is the difference between the State's total assessed expenditure (expenses and investment) and the sum of its own source revenue, net borrowing and Commonwealth payments.

[1] The procedure used by the Commission to derive the recommended GST distribution using State revenue, expenditure and payments for specific purposes (PSPs) is called the distribution model. Information about the distribution model is available on the Commission's website (https://cgc.gov.au/).

Figure 1 Illustrative assessed budgets per capita, 2018-19



(a) Includes expenses and investment.
Source: Commission calculation.

4 Differences in State fiscal capacities have reduced in this update, resulting in a decline in the proportion of GST revenue redistributed away from EPC to the States with below average fiscal capacities from 12.5% ($7.8 billion) to 10.4% ($6.8 billion). The magnitude of the improvements in the fiscal capacities of Queensland and the Northern Territory is such that, even taking into account growth in the GST pool, their recommended GST entitlements are lower in 2018-19 than in 2017-18.

MOVEMENTS IN THE GST DISTRIBUTION

5 Table 2 shows the differences between the estimated GST distribution for 2017-18 and the illustrative distribution for 2018-19. Changes have occurred for a number of reasons:

- estimated State populations between 2017-18 and 2018-19 have changed
- the amount of GST revenue available for distribution has increased
- the relative fiscal capacities of the States have changed mainly because of changes in State circumstances.

6 The Commission's work focuses on the last factor — assessment of the changes in States' fiscal capacities.

Table 2 Distribution of the 2017-18 GST and illustrative 2018-19 GST distribution

	NSW	Vic	Qld	WA	SA	Tas	ACT	NT	Total
	$m	$m	$m	$m	$m	$m	$m	$m	$m
Estimated 2017-18	17 511	14 989	14 848	2 255	6 284	2 378	1 244	2 891	62 400
Illustrative 2018-19 (a)	18 030	16 830	14 447	3 255	6 751	2 434	1 298	2 755	65 800
Change	520	1 841	-401	999	467	56	53	-136	3 400
Change caused by new:									
Population (b)	16	90	-2	-8	-44	-21	1	-33	0
Pool (c)	955	822	809	122	340	128	68	156	3 400
Fiscal capacities (d)	-451	929	-1 208	885	172	-52	-15	-260	0
Change ($m)	520	1 841	-401	999	467	56	53	-136	3 400
Change ($pc)	65	283	-80	381	268	107	128	-553	135

(a) Obtained by applying the 2018 Update relativities to estimated State populations as at December 2018 and estimated GST revenue for 2018-19.

(b) Effects on the distribution of 2017-18 GST revenue of using projected State populations as at December 2018 instead of December 2017, with 2017 Update relativities.

(c) Effect of applying the 2017 Update relativities to the estimated growth in GST revenue for 2018-19.

(d) Effects on the distribution of the 2018-19 GST revenue of using the 2018 Update fiscal capacities instead of 2017 Update fiscal capacities.

Source: 2017-18 GST entitlement and 2018-19 GST revenue are taken from the *Australian Government Budget, Mid-Year Economic and Fiscal Outlook 2017-18.* December 2017 and 2018 population estimates were provided by the Commonwealth Treasury.

WHY STATE FISCAL CAPACITIES HAVE CHANGED

7 The Commission assesses fiscal capacities based on a rolling average of three years. In this update, revisions were first made to data used in the 2017 Update, including incorporating revisions to Australian Bureau of Statistics (ABS) population estimates following the 2016 Census. Then, consistent with the terms of reference, the Commission added data for 2016-17 to its calculations and removed data for 2013-14. The differences between these years are the major influence on changes in measured State fiscal capacities.

8 The Commission has recommended a changed distribution for 2018-19 because new data reveal changes in fiscal capacities in all areas of State budgets, as shown in Table 3. Changes in States' estimated revenue raising capacities have been much more significant than changes in other aspects of State budgets.

Table 3 Change in fiscal capacities by source of change, 2018-19

	NSW	Vic	Qld	WA	SA	Tas	ACT	NT	Redist (a)
	$m	$m	$m	$m	$m	$m	$m	$m	$m
Expense requirement	189	145	-486	148	108	15	5	-124	610
Investment requirement	291	630	-218	-621	-60	9	36	-67	966
Net borrowing	-8	-90	16	82	3	0	-5	3	104
Revenue capacity	-841	-283	-272	1 287	202	-42	-69	17	1 506
Commonwealth payments	-82	528	-250	-11	-82	-33	18	-88	546
Total	-451	929	-1 208	885	172	-52	-15	-260	1 986

Note: The total change shown here, from 2017-18 to 2018-19, is equivalent to the change caused by new fiscal capacities shown in Table 2.
(a) The redistribution is calculated as half the absolute sum of the items in the row.
Source: Commission calculation.

9 Table 4 shows the main causes of the change in the GST distribution. They are listed in order of importance.

Table 4 Causes of change in the GST distribution, 2018-19

	NSW	Vic	Qld	WA	SA	Tas	ACT	NT	Redist
	$m	$m	$m	$m	$m	$m	$m	$m	$m
Mining production	-194	-86	-417	669	44	-13	-6	3	716
Natural disaster relief	362	92	-545	50	41	17	8	-24	569
Population growth	107	427	-102	-410	-30	11	16	-19	560
Commonwealth payments	-82	528	-250	-11	-82	-33	18	-88	546
Property sales	-250	-129	-69	401	36	-5	-13	29	466
Socio-economic status	-298	-15	145	124	53	15	9	-34	346
Taxable payrolls	-113	-110	74	149	88	-23	-53	-12	310
Wage costs	-94	145	90	-126	-2	-18	15	-9	250
Taxable land values	-220	-16	121	75	29	6	5	1	236
All other changes	331	92	-256	-35	-6	-7	-14	-105	423
Total	-451	929	-1 208	885	172	-52	-15	-260	1 986

Source: Commission calculation.

10 The most important changes were as follows.

- ***Mining production.*** Between 2013-14 and 2016-17, the value of iron ore production fell, while the value of coal production rose. These changes increased the fiscal capacities of New South Wales and Queensland and reduced their GST shares. The changes reduced the fiscal capacity of Western Australia. Its fiscal capacity was further reduced by declining North West Shelf royalties. As a result, Western Australia's GST share increased.
- ***Natural disaster relief.*** The net expenses for Queensland and the Northern Territory were significantly lower in 2016-17 compared with 2013-14,

resulting in a decline in their GST shares and increases in the GST shares of other States.

- ***Population growth.*** The pattern of population growth has changed between 2013-14 and 2016-17, leading to a change in the pattern of investment requirements among the States. The rate of population growth in some States has declined, particularly in Western Australia and the Northern Territory, while it has increased in New South Wales, Victoria, Tasmania and the ACT. This increased the investment requirements of the latter States and hence their GST shares.
- ***Commonwealth payments.*** There were significant changes in the size and distribution of payments among the States in 2016-17 compared with 2013-14. A reduction in Victoria's share of payments for road and rail infrastructure increased its GST share. In contrast, an increase in the share of these payments received by New South Wales, Queensland, South Australia and Tasmania reduced their GST shares. Increases in the share of National Health Reform funding received by Queensland, Western Australia and Tasmania reduced their GST shares. The Northern Territory's share of Commonwealth payments increased over the period, particularly for health, government schools and remote Indigenous housing. This resulted in a reduction in its GST share. The use of new Census data and the cessation of backcasting for Students First funding also had an impact on States' GST shares.
- ***Property sales.*** Between 2013-14 and 2016-17, shares of total property sales for each of Western Australia, South Australia and the Northern Territory fell. This reduced their revenue raising capacities and increased their GST share. The GST shares of other States correspondingly fell.
- ***Socio-economic status.*** Changes to the socio-economic status of State populations between the 2011 Census and the 2016 Census affected their relative costs of providing services. Data from the 2016 Census indicated that New South Wales and the Northern Territory had a relatively higher proportion of their population in the least disadvantaged non-Indigenous areas compared with 2011, reducing their expense requirement and their GST shares. In contrast, Western Australia and, to a lesser extent, Queensland, South Australia and the ACT were found to be more disadvantaged than they had been in 2011, increasing the GST share of these States.
- ***Taxable payrolls.*** Differences between States in the rate of growth of taxable payrolls between 2013-14 and 2016-17 affected States' revenue raising capacities. Above average growth in taxable payrolls in New South Wales, Victoria, Tasmania, the ACT and the Northern Territory increased their revenue raising capacities and reduced their GST shares. Taxable payrolls in Queensland, Western Australia and South Australia grew by less than the average over the period, resulting in a decrease in their revenue raising capacities and an increase in their GST shares.

- ***Wage costs.*** Relative wage costs outside the control of State governments increased faster than average in Victoria, Queensland and the ACT between 2013-14 and 2016-17. This increased their relative costs of service provision and their GST shares. Below average wage growth in the other States reduced their relative costs of service provision and their GST shares.
- ***Taxable land values.*** Between 2013-14 and 2016-17, New South Wales' share of total taxable land values grew, increasing its revenue raising capacity and reducing its GST share. In contrast, Queensland's and Western Australia's share of taxable land values declined, reducing their revenue raising capacity and increasing their GST shares.

STATE BY STATE CHANGES SINCE THE 2017 UPDATE

11 Changes that have had important effects on the assessed fiscal capacity of each State are summarised in this section. These changes can occur because more recent economic and demographic circumstances are being reflected in States' GST shares (referred to as changes in circumstances), or because historical data used in assessments have been revised (referred to as revisions). For most States, the largest causes of change in GST shares in this update have been changes in circumstances.

12 The effects of incorporating the 2016 Census data (and associated changes to populations) are included with data revisions in this section. While the impact of new Census data is shown separately in the main changes table for each State, incorporating new Census data has also affected the size of the other changes shown in those tables. Chapter 1 provides more detail on the changes in this update, including the impact of data revisions excluding Census related effects.

New South Wales

Changes in this update. New South Wales has the second highest fiscal capacity. Strong growth in property sales, land values, mining production and taxable payrolls improved its revenue raising capacity and reduced its GST share. These changes were partially offset by an increase in its net natural disaster relief expenses. New South Wales' increased fiscal capacity will see its GST share fall from 28.1% to 27.4%. Despite a net increase in its fiscal capacity, its GST entitlement in 2018-19 will rise by $520 million, or 3.0%, due to growth in the pool.

Table 5 Change in GST

	$m	$pc
Change due to		
New population	16	2
Growth in GST available	955	119
New relativities	-451	-56
Data revisions	*-16*	*-2*
Change in circumstances	*-435*	*-54*
Total change	520	65

Note: Table may not add due to rounding.

Table 6 Main changes for New South Wales

$m	Reason for change
362	**Natural disaster relief.** New South Wales' share of net natural disaster relief expenses was higher in 2016-17 compared to 2013-14, resulting in an increase in its GST share.
-250	**Property sales.** Above average growth in property sales increased New South Wales' capacity to raise revenue from conveyance duty and reduced its GST share.
-220	**Taxable land values.** Above average growth in land values increased the State's share of taxable land values and reduced its GST share.
-194	**Mining production.** An increase in the total value of coal production, combined with a fall in the total value of iron ore production, increased the State's relative revenue raising capacity and reduced its GST share.
-113	**Taxable payrolls.** Above average growth in taxable payrolls increased New South Wales' capacity to raise revenue and reduced its share of GST.
-373	**New Census data.** The 2016 Census found New South Wales' non-Indigenous population to be less disadvantaged than it had been in 2011, reducing its assessed service delivery costs and its GST share.

Fiscal capacity. New South Wales' strong fiscal capacity is due to its below average assessed costs of providing services, reflecting the State's below average share of people living in remote areas, above average non-State provision of health services, and economies of scale in administration. It also has an above average capacity to raise revenue, with a high value of property sales, high land values and above average taxable payrolls.

Those effects on its fiscal capacity are partly offset by the State's above average requirement for investment and a below average share of Commonwealth payments.

Table 7 Assessed GST, 2018-19

	$m	$pc
Equal per capita share	21 052	2 622
Effect of assessed:		
Expenses	-2 428	-302
Investment	333	41
Net borrowing	8	1
Revenue	-956	-119
Commonwealth payments	22	3
Assessed GST	18 030	2 246

Note: Table may not add due to rounding.

Victoria

Changes in this update. Victoria's assessed fiscal capacity has fallen but remains the third highest. Its expenditure requirement is higher due to an increase in its investment requirement, driven by strong population growth, as well as an increase in its relative wage costs. A smaller share of Commonwealth payments also increased its GST share. These changes were partly offset by a relative fall in Victoria's cost of providing school education and strong property sales. Compared with 2017-18, the State's share of the GST will rise from 24.0% to 25.6%. Its lower relative fiscal capacity, together with growth in the pool, will see its GST entitlement rise by $1 841 million, or 12.3%.

Table 8 Change in GST

	$m	$pc
Change due to		
New population	90	14
Growth in GST available	822	126
New relativities	929	143
Data revisions	*412*	*63*
Change in circumstances	*518*	*80*
Total change	1 841	283

Note: Table may not add due to rounding.

Table 9 Main changes for Victoria

$m	Reason for change
528	**Commonwealth payments.** Victoria's share of payments was lower in 2016-17 than in 2013-14, mainly due to road and rail infrastructure payments. This increased its GST share.
427	**Population growth.** Increases in Victoria's share of national population growth increased its investment requirements and its GST share.
-149	**School education.** Census based upward revisions to its total population mean that, with no revisions to student numbers, Victoria's students per capita have been revised downward, reducing its GST share.
145	**Wage costs.** Above average growth in Victorian wage levels increased its service delivery costs and its GST share.
-129	**Property sales.** Above average growth in property sales increased the State's capacity to raise revenue from conveyance duty and reduced its GST share.
578	**New Census data.** Upward revisions to Victoria's total population associated with the 2016 Census decreased its relative revenue raising capacity and increased its GST share.

Fiscal capacity. Victoria's strong fiscal capacity is due to its well below average assessed costs of providing services, reflecting its below average shares of government school enrolments, Indigenous people and people living in remote areas. This is reduced further by economies of scale in administration and below average wage costs.

Those effects on its fiscal capacity are partly offset by its below average revenue raising capacity, which is mainly due to its below average mining production and taxable payrolls, and by its above average investment requirements due to above average share of national population growth.

Table 10 Assessed GST, 2018-19

	$m	$pc
Equal per capita share	17 031	2 622
Effect of assessed:		
Expenses	-4 972	-765
Investment	1 254	193
Net borrowing	-182	-28
Revenue	2 882	444
Commonwealth payments	817	126
Assessed GST	16 830	2 591

Note: Table may not add due to rounding.

Queensland

Changes in this update. Queensland has the fourth highest fiscal capacity. Its assessed fiscal capacity has strengthened due to a decrease in its net natural disaster relief expenses, and increases in its share of Commonwealth payments and its relative capacity to raise mining royalties from coal production. In addition, a decrease in its share of national population growth reduced its investment needs. Compared with 2017-18, the State's GST share will fall from 23.8% to 22.0%. Growth in the pool does not offset the impact of Queensland's improved fiscal capacity, and its GST entitlement will fall by $401 million, or 2.7%.

Table 11 Change in GST

	$m	$pc
Change due to		
New population	-2	0
Growth in GST available	809	161
New relativities	-1 208	-241
Data revisions	*-21*	*-4*
Change in circumstances	*-1 187*	*-236*
Total change	-401	-80

Note: Table may not add due to rounding.

Table 12 Main changes for Queensland

$m	Reason for change
-545	**Natural disaster relief.** Queensland's net natural disaster expenses were almost $1.5 billion lower in 2016-17 compared to 2013-14, resulting in a decline in its GST share. The high net expenses in 2013-14 were the result of a number of major flood and cyclone events between 2011 and 2014.
-417	**Mining production.** An increase in the total value of coal production, combined with a fall in the total value of iron ore production, increased Queensland's relative revenue raising capacity and reduced its GST share.
-250	**Commonwealth payments.** Queensland's share of payments was greater in 2016-17 than in 2013-14, mainly due to road and rail infrastructure payments. This reduced its GST share.
121	**Taxable land values.** Below average growth in land values reduced the State's share of taxable land values and increased its GST share.
-102	**Population growth.** Queensland's population growth has slowed. This, in conjunction with revisions to its share of population growth, has led to a reduction in Queensland's assessed need for investment.
56	**New Census data.** The 2016 Census found Queensland's non-Indigenous population to be more disadvantaged than it had been in 2011, increasing its service delivery costs and its GST share.

Fiscal capacity. Queensland's below average fiscal capacity is due to above average assessed expenses and below average revenue raising capacity reflecting its below average taxable payrolls, property sales and taxable land values. This is partly offset by its above average mining production and an above average share of Commonwealth payments.

Its high expense requirements are due to above average shares of government school enrolments, Indigenous people and people living in remote areas. In addition, Queensland's share of net natural disaster relief expenses is well above average. Those effects are partly offset by its below average wage expenses and costs of providing urban transport.

Table 13 Assessed GST, 2018-19

	$m	$pc
Equal per capita share	13 164	2 622
Effect of assessed:		
Expenses	1 605	320
Investment	-426	-85
Net borrowing	27	5
Revenue	583	116
Commonwealth payments	-505	-101
Assessed GST	14 447	2 878

Note: Table may not add due to rounding.

Western Australia

Changes in this update. Western Australia remains the State with the strongest fiscal capacity. However, its assessed fiscal capacity is declining, resulting in its share of GST revenue in 2018-19 increasing from 3.6% to 4.9%. This is primarily the result of a decline in its revenue raising capacity, due to a fall in the value of iron ore production and below average growth in property sales and taxable payrolls. This is partly offset by a decline in its share of national population growth, that reduced its investment requirement, and by below average growth in wage levels. Compared with 2017-18, the State's GST will rise by $999 million, or 44.3%.

Table 14 Change in GST

	$m	$pc
Change due to		
New population	-8	-3
Growth in GST available	122	47
New relativities	885	338
Data revisions	*-367*	*-140*
Change in circumstances	*1 252*	*478*
Total change	999	381

Note: Table may not add due to rounding.

Table 15 Main changes for Western Australia

$m	Reason for change
669	**Mining production.** A fall in the value of iron ore production, and a decline in North West Shelf royalties, reduced Western Australia's relative revenue raising capacity and increased its share of GST.
-410	**Population growth.** Decreases in its share of national population growth have reduced Western Australia's requirements for investment and its GST share.
401	**Property sales.** Below average increase in property sales reduced the State's capacity to raise revenue from conveyance duty and increased its share of GST.
149	**Taxable payrolls.** Below average growth in taxable payrolls between 2013-14 and 2016-17 reduced Western Australia's revenue raising capacity and increased its GST share.
-126	**Wage costs.** Below average growth in wage levels reduced Western Australia's assessed service delivery costs and its GST share.
-311	**New Census data.** Downward revisions to Western Australia's total population associated with the 2016 Census increased its relative revenue raising capacity and decreased its GST share.

Fiscal capacity. Western Australia's high fiscal capacity is due to above average capacity in all revenue streams except stamp duty and insurance tax. It has especially high capacity in mining revenue and, to a lesser extent, taxable payrolls. The effects on its fiscal capacity are partly offset by its having the third highest assessed expenses per capita.

Its high expense requirements are due to above average shares of Indigenous people and people in remote areas. Above average wage levels and below average non-State provision of health services also contribute to its relatively high assessed expense needs.

Table 16 Assessed GST, 2018-19

	$m	$pc
Equal per capita share	6 873	2 622
Effect of assessed:		
Expenses	2 324	886
Investment	-485	-185
Net borrowing	70	27
Revenue	-5 531	-2 110
Commonwealth payments	5	2
Assessed GST	3 255	1 242

Note: Table may not add due to rounding.

South Australia

Changes in this update. South Australia's fiscal capacity, which remains the third lowest, has deteriorated slightly, mainly due to slow growth in taxable payrolls and property sales, and a decline in its share of mining production. In addition, an increase in its share of net natural disaster relief expenses has increased its GST requirement. This was partly offset by an increase in its share of Commonwealth payments, which reduced South Australia's GST. Compared with 2017-18, the State's share of GST will rise from 10.1% to 10.3% and, combined with pool growth, its GST entitlement will rise by $467 million, or 7.4%.

Table 17 Change in GST

	$m	$pc
Change due to		
New population	-44	-26
Growth in GST available	340	195
New relativities	172	99
Data revisions	*84*	*48*
Change in circumstances	*87*	*50*
Total change	467	268

Note: Table may not add due to rounding.

Table 18 Main changes for South Australia

$m	Reason for change
88	**Taxable payrolls.** Below average growth in taxable payrolls reduced South Australia's capacity to raise revenue and increased its share of GST.
-82	**Commonwealth payments**. South Australia's share of payments was greater in 2016-17 than in 2013-14, mainly due to road infrastructure payments. This reduced its GST share.
44	**Mining production.** An increase in the total value of production of coal, combined with a fall in the total value of production of other minerals, reduced South Australia's relative revenue raising capacity and increased its GST share.
41	**Natural disaster relief.** South Australia's share of net natural disaster expenses was higher in 2016-17 than in 2013-14, resulting in an increase in its GST share.
36	**Property sales.** Below average growth in property sales reduced South Australia's capacity to raise revenue from conveyance duty and increased its share of GST.
2	**New Census data.** The 2016 Census found South Australia's non-Indigenous population to be more disadvantaged than it had been in 2011, marginally increasing its assessed service delivery costs and its GST share.

Fiscal capacity. South Australia's below average fiscal capacity is mainly due to its below average revenue raising capacity from property sales, mining royalties, taxable payrolls, and land tax. It also receives below average revenue from Commonwealth payments.

Those effects are reinforced by its above average expense requirement, which reflects its above average shares of older people and people of low socio-economic status, offset partially by below average wage expenses and assessed transport costs.

Its above average requirement for GST is partially offset by its below average share of national population growth, leading to below average assessed investment.

Table 19 Assessed GST, 2018-19

	$m	$pc
Equal per capita share	4 563	2 622
Effect of assessed:		
Expenses	472	271
Investment	-332	-191
Net borrowing	47	27
Revenue	1 932	1 110
Commonwealth payments	69	39
Assessed GST	6 751	3 879

Note: Table may not add due to rounding.

Tasmania

Changes in this update. Tasmania remains the State with the second lowest fiscal capacity. Its GST requirement fell due to an increase in its share of Commonwealth payments and a relative increase in its taxable payrolls and an increase in its share of mining production. This was reinforced by a decline in Tasmania's relative wage costs. These changes were partly offset by a relative increase in its net natural disaster relief expenses. While Tasmania's increased fiscal capacity will see its GST share fall from 3.8% to 3.7%, its GST entitlement in 2018-19 will rise by $56 million, or 2.4%, due to growth in the pool.

Table 20 Change in GST

	$m	$pc
Change due to		
New population	-21	-39
Growth in GST available	128	245
New relativities	-52	-98
Data revisions	*-6*	*-12*
Change in circumstances	*-45*	*-86*
Total change	56	107

Note: Table may not add due to rounding.

Table 21 Main changes for Tasmania

$m	Reason for change
-33	**Commonwealth payments.** Tasmania's share of payments was greater in 2016-17 than in 2013-14, mainly due to road infrastructure payments. This reduced its GST share. The cessation of backcasting Students First funding also contributed to its reduced GST share.
-23	**Taxable payrolls.** Above average growth in taxable payrolls between 2013-14 and 2016-17 increased Tasmania's revenue raising capacity and decreased its GST share.
-18	**Wage costs.** Below average growth in wage levels reduced its assessed service delivery costs and its GST share.
17	**Natural disaster relief.** Tasmania's natural disaster relief net expenses were higher in 2016-17 compared with 2013-14 due to flood and bushfire events in 2016, increasing its GST share.
-13	**Mining production.** Above average growth in the value of production of other minerals between 2013-14 and 2016-17 increased Tasmania's revenue raising capacity and decreased its GST share.
5	**New Census data.** Tasmania's Indigenous population is relatively more disadvantaged than in 2011, increasing its assessed service delivery costs and its GST share.

Fiscal capacity. Tasmania has the weakest revenue capacity in most tax bases, with well below average taxable payrolls and property sales. In addition, it has the second highest per capita assessed expenses for health and welfare.

These high service delivery costs reflect the State's above average shares of people in regional areas and people of low socio-economic status, older people and government school students. These higher assessed costs are compounded by diseconomies of scale in administration.

Table 22 Assessed GST, 2018-19

	$m	$pc
Equal per capita share	1 375	2 622
Effect of assessed:		
Expenses	537	1 023
Investment	-159	-303
Net borrowing	22	43
Revenue	717	1 367
Commonwealth payments	-58	-111
Assessed GST	2 434	4 640

Note: Table may not add due to rounding.

Australian Capital Territory

Changes in this update. The ACT's fiscal capacity, which remains the fourth lowest, has improved due to an increase in its relative revenue raising capacity. Above average growth in property sales and an upward revision to its payroll tax base reduced its GST requirement. These changes were partly offset by a decrease in its share of Commonwealth payments and an increase in its share of national population growth, which increased its investment requirement. It also had above average growth in wage costs. As in 2017-18, the ACT's share of GST remains at 2.0%. Its GST entitlement will rise by $53 million, or 4.3%, due to growth in the pool.

Table 23 Change in GST

	$m	$pc
Change due to		
New population	1	3
Growth in GST available	68	162
New relativities	-15	-37
Data revisions	*-25*	*-59*
Change in circumstances	*9*	*22*
Total change	53	128

Note: Table may not add due to rounding.

Table 24 Main changes for the ACT

$m	Reason for change
-53	**Taxable payrolls.** Upward revisions to ABS data on compensation of employees, combined with above average growth between 2013-14 and 2016-17, increased the ACT's revenue raising capacity and reduced its GST share.
18	**Commonwealth payments.** The ACT's share of payments was lower in 2016-17 than in 2013-14, increasing its GST share.
16	**Population growth.** Data from the 2016 Census population have led to upward revisions to estimates of the ACT's population growth, and therefore to the ACT's GST share.
15	**Wage costs.** Above average growth in wage levels increased the ACT's assessed service delivery costs and its GST share.
-13	**Property sales.** Above average growth in property sales increased the ACT's capacity to raise revenue from conveyance duty and reduced its GST share.
43	**New Census data.** Upward revisions to the ACT's total population associated with the 2016 Census reduced its revenue raising capacity and increased its GST share.

Fiscal capacity. The ACT's below average fiscal capacity is due to its below average capacity to raise revenue across all revenue bases. It has no mining industry and low revenue raising capacity from land values, stamp duty and taxable payrolls. It also receives a below average share of Commonwealth payments.

The ACT's assessed cost of providing services is also below average, partially offsetting its low revenue raising capacity. The low cost of its relatively young, urbanised, higher socio-economic status population more than offsets the impact of diseconomies of scale in administration and above average wage costs.

Table 25 Assessed GST, 2018-19

	$m	$pc
Equal per capita share	1 098	2 622
Effect of assessed:		
Expenses	-194	-463
Investment	-20	-47
Net borrowing	-3	-7
Revenue	332	794
Commonwealth payments	85	202
Assessed GST	1 298	3 100

Note: Table may not add due to rounding.

Northern Territory

Changes in this update. The Northern Territory's fiscal capacity has strengthened markedly, but it remains the fiscally weakest State. An increased share of Commonwealth payments reduced its GST requirement, as did a lower investment requirement resulting from changes in total investment in urban transport and rural roads. These changes were reinforced by declining spending on utility subsidies across all States, and an increase in urban transport investment. The Northern Territory's increased fiscal capacity will see its GST share in 2018-19 fall from 4.6% to 4.2%. Growth in the pool does not offset the impact of the Northern Territory's improved fiscal capacity and, therefore, its GST entitlement will fall by $136 million, or 4.7%.

Table 26 Change in GST

	$m	$pc
Change due to		
New population	-33	-132
Growth in GST available	156	632
New relativities	-260	-1 054
Data revisions	*-61*	*-247*
Change in circumstances	*-199*	*-807*
Total change	-136	-553

Note: Table may not add due to rounding.

Table 27 Main changes for the Northern Territory

$m	Reason for change
-88	**Commonwealth payments.** The Northern Territory's share of payments was greater in 2016-17 than in 2013-14, mainly due to health, government schools and remote Indigenous housing payments. This reduced its GST share.
-33	**Investment growth.** Nationally, a large increase in investment in urban transport, for which the Northern Territory has below average needs, combined with a large decrease in investment in rural roads, where the Northern Territory has above average needs, decreased its GST share.
29	**Property sales.** Below average growth in property sales reduced its capacity to raise revenue from conveyance duty and increased its share of GST.
-25	**Small communities.** Total State spending on utility subsidies declined between 2013-14 and 2016-17. As a result, States with a relatively high proportion of their population living in small remote communities, including the Northern Territory, were assessed as needing to spend less on utility subsidies.
-24	**Natural disaster relief.** The Northern Territory revised upwards 2014-15 and 2015-16 NDRRA revenue from the Commonwealth resulting in a decline in its net expenses. This reduced its GST share.
0	**New Census data.** The 2016 Census found the Northern Territory's non-Indigenous population to be less disadvantaged than it had been in 2011. This was offset by an increase in the public housing use rate by Indigenous people in remote areas.

Fiscal capacity. The Northern Territory's below average fiscal capacity is primarily due to its above average assessed expenses. It has above average shares of a range of high cost population groups, including exceptionally high proportions of Indigenous people and people in remote areas.

The Northern Territory has below average revenue raising capacity for most revenue streams. Its above average need for assistance is partially met through an above average share of Commonwealth payments.

Table 28 Assessed GST, 2018-19

	$m	$pc
Equal per capita share	646	2 622
Effect of assessed:		
Expenses	2 657	10 784
Investment	-165	-671
Net borrowing	11	45
Revenue	40	162
Commonwealth payments	-434	-1 761
Assessed GST	2 755	11 181

Note: Table may not add due to rounding.

CHAPTER 1

CHANGES IN THE GST DISTRIBUTION

1.1 This chapter explains why the GST distribution in this update differs from the 2017 Update distribution.

MOVEMENTS IN THE GST DISTRIBUTION

1.2 Table 1-1 shows the differences between the estimated GST distribution for 2017-18 and the illustrative distribution for 2018-19.

Table 1-1 Distribution of the 2017-18 GST and the illustrative 2018-19 GST distribution

	NSW	Vic	Qld	WA	SA	Tas	ACT	NT	Total
	$m	$m	$m	$m	$m	$m	$m	$m	$m
Estimated 2017-18	17 511	14 989	14 848	2 255	6 284	2 378	1 244	2 891	62 400
Illustrative 2018-19 (a)	18 030	16 830	14 447	3 255	6 751	2 434	1 298	2 755	65 800
Change	520	1 841	-401	999	467	56	53	-136	3 400
Change caused by new:									
Population (b)	16	90	-2	-8	-44	-21	1	-33	0
Pool (c)	955	822	809	122	340	128	68	156	3 400
Fiscal capacities (d)	-451	929	-1 208	885	172	-52	-15	-260	0
Change ($m)	520	1 841	-401	999	467	56	53	-136	3 400
Change ($pc)	65	283	-80	381	268	107	128	-553	135

(a) Obtained by applying the 2018 Update relativities to estimated State populations as at December 2018 and estimated GST revenue for 2018-19.
(b) Effects on the distribution of 2017-18 GST revenue of using projected State populations as at December 2018 instead of December 2017, with 2017 Update relativities.
(c) Effect of applying the 2017 Update relativities to the estimated growth in GST revenue for 2018-19.
(d) Effects on the distribution of the 2018-19 GST revenue of using the 2018 Update fiscal capacities instead of 2017 Update fiscal capacities.
Source: 2017-18 GST entitlement and 2018-19 GST revenue are taken from the *Australian Government Budget, Mid-Year Economic and Fiscal Outlook 2017-18.* December 2017 and 2018 population estimates were provided by the Commonwealth Treasury.

1.3 The two distributions differ for the following reasons.

- State populations have changed — the illustrative 2018-19 distribution is based on projected State populations as at December 2018 whereas the 2017-18 distribution is based on populations for a year earlier. State shares of the total population differ slightly between these two dates and affect the total GST allocation for each State.

- The size of the GST pool available for distribution has changed. Any growth in the pool is distributed among States using their relativity weighted population shares.
- The relativities used to distribute the GST have changed, reflecting changes in the assessed fiscal capacities of States. The illustrative 2018-19 distribution is based on the relativities recommended in this report whereas the 2017-18 distribution is based on relativities derived in the 2017 Update and subsequently adopted by the Treasurer on 27 April 2017.[2]

1.4 The Commission's work affects only the changes in the relativities which the Commission derives from its assessment of State fiscal capacities.

Why State fiscal capacities change between updates

1.5 The total change in State fiscal capacities can be attributed to changes in Commonwealth payments for specific purposes, as well as changes in the Commission's assessments of revenue raising capacity and requirement to provide services and infrastructure. These changes occur for the following reasons.

- They reflect more recent economic and demographic circumstances of the States. The 2018 Update relativities are based on an average of data for 2014-15 to 2016-17, whereas the 2017 Update relativities were based on data for 2013-14 to 2015-16. Differences between the year brought into the three year average (2016-17 for this update) and the year deleted (2013-14) change the relativities. However, the three year averaging process means changes in circumstances have a gradual effect.
- Data used in the assessments in the 2017 Update may be revised. Revisions occur because new data become available. Revisions can also occur because data providers identify errors in their data or because of errors made by the Commission in previous inquiries.

1.6 Table 1-2 shows that changes in State circumstances have been the major cause of the change in the redistribution for most States. The main data revisions and changes in circumstances are discussed below.

1.7 In addition to revisions and changes in circumstances, *s*ubject to consultation with Commonwealth and State governments, the assessment methods may be varied if considered necessary to better reflect the current financial arrangements between the Commonwealth and State governments, or to overcome problems in the data used previously. In this update, cessation of backcasting associated with the Schools assessment was a method change (refer to Chapter 2 for further details of this change).

2 References to changes over time generally reflect the change over the assessment years, from dropping 2013-14 and including 2016-17. They are not intended to imply current or prospective movements.

Table 1-2 Change in GST distribution by source of change, 2018-19

	NSW	Vic	Qld	WA	SA	Tas	ACT	NT	Redist (a)
	$m	$m	$m	$m	$m	$m	$m	$m	$m
Data revisions	-16	412	-21	-367	84	-6	-25	-61	496
Change in circumstances	-435	518	-1 187	1 252	87	-45	9	-199	1 866
Total	-451	929	-1 208	885	172	-52	-15	-260	1 986

(a) The redistribution is calculated as half the absolute sum of the items in the row.
Source: Commission calculation.

1.8 Detailed tables on the changes resulting from each of the Commission's assessments can be found in the supporting information for this update which is available on the Commission's website (https://cgc.gov.au/).

DATA REVISIONS

1.9 Data revisions for the three years of the 2017 Update changed the redistribution by $496 million in this update. The largest sources of revision are shown in Table 1-3. They relate to the following.

- ***New Census data.*** The effects of incorporating data from the 2016 Census, and associated changes to population data, are classified as data revisions. These effects are described in Box 1-1.
- ***Taxable payrolls.*** Revisions to the ABS Compensation of Employees (CoE) data redistributed $183 million, increasing the GST shares of New South Wales, Western Australia and South Australia. Upward revisions to the data for the ACT, particularly for 2014-15 and 2015-16, redistributed $44 million away from it. The Commission considers that, while these revisions may result from statistical processes used by the ABS in compiling the CoE data, the use of these data is consistent with the 2015 Review methodology and with the terms of reference requirement to use the latest available data.
- ***Property sales.*** Replacing States' uniform presentation framework (UPF) data for 2015-16 with ABS Government Finance Statistics (GFS) data resulted in downward revisions to conveyance duty for New South Wales and the Northern Territory. This reduced their fiscal capacity and increased their GST shares.
- ***Commonwealth payments.*** The cessation of backcasting of the Students First payment increased the GST shares of New South Wales, Queensland and Western Australia, and decreased the GST shares for other States. The correction of an error for rail infrastructure payments had a small impact on GST redistribution, decreasing the GST shares of New South Wales and Tasmania and increasing the GST shares of other States.

Table 1-3 Main effects of data revisions, 2018 Update

	NSW	Vic	Qld	WA	SA	Tas	ACT	NT	Redist
	$m	$m	$m	$m	$m	$m	$m	$m	$m
New Census data	-373	578	56	-311	2	5	43	0	684
Taxable payrolls	74	-104	-24	41	68	-10	-44	0	183
Property sales	117	-47	-37	-19	-12	-4	-3	5	122
Commonwealth payments	3	-34	49	46	-28	-19	-5	-12	98
Other revisions	163	19	-66	-123	54	22	-15	-55	259
Total	-16	412	-21	-367	84	-6	-25	-61	496

Note: Census related revisions are shown separately in this table. The other revisions shown in this table exclude any effects of Census related revisions.

Source: Commission calculation.

Box 1-1 Effect of incorporating 2016 Census data

Total population. One of the most significant implications of the 2016 Census is that the estimates of Victoria's population have been revised upward by 111 000, while Western Australia's population estimates have been revised downward by about 58 000. The table below shows that these changes redistributed $595 million, increasing Victoria's GST share and reducing Western Australia's GST share, largely reflecting a relative decline and increase in these States' respective per capita revenue raising capacities.

Indigenous population. In addition to revisions to total population levels, the 2016 Census provided more recent information on the attributes of the population. Between the 2011 and 2016 Censuses, State shares of the Indigenous population changed. New South Wales' Indigenous population estimate for 2016 was revised upward by 15%, mainly in the less disadvantaged non-remote areas. New South Wales' share of that population increased, while Queensland's share decreased. Western Australia's share of the total Indigenous population fell slightly, but its share of the remote Indigenous population increased. Similarly to Western Australia, while the Northern Territory's share of the total Indigenous population has fallen, its share of the remote Indigenous population has increased slightly. (Box 1-2 describes the Commission's methods for assessing Indigenous needs, in particular how they deal with the heterogeneity of the Indigenous population and its changing attributes.) The effect of revised Indigenous populations and attributes associated with the 2016 Census has reduced Queensland and the Northern Territory's GST shares by about $90 million and $12 million respectively and increased that of New South Wales ($35 million), Victoria ($39 million), Western Australia ($22 million) and Tasmania ($20 million).

Socio-economic status of the non-Indigenous population. Between 2011 and 2016, the socio-economic profile of Australia changed. New South Wales and the Northern Territory had a greater proportion of their population in the least disadvantaged non-Indigenous areas in 2016 than in 2011. Western Australia and, to a lesser extent, Queensland, South Australia and the ACT were found to be more disadvantaged than they had been in the 2011 Census. This decreased New South Wales' GST share by about $300 million, and increased the GST shares of Queensland and Western Australia. The 2016 Census also resulted in revisions to the age structure and geographic distribution of the population in each State. In total, changes related to the 2016 Census redistributed $684 million, mainly to Victoria, and away from New South Wales and Western Australia, as shown in the table below.

Effects of revisions associated with the 2016 Census

	NSW	Vic	Qld	WA	SA	Tas	ACT	NT	Redist
	$m	$m	$m	$m	$m	$m	$m	$m	$m
Population levels	-9	532	-65	-510	18	12	32	-12	595
Population composition	-364	46	121	199	-15	-8	10	12	387
Total change	-373	578	56	-311	2	5	43	0	684

Source: Commission calculation.

Box 1-2 Indigenous disadvantage and the GST

For those services where Indigenous status is a major influence on State spending, the Commission has estimated that States spend $19 000 per Indigenous person, and $6 200 per non-Indigenous person. This is largely because Indigenous people use a range of State services more frequently, or more intensively, than non-Indigenous people. It is also because Indigenous people are more likely to live in remote areas, where costs are higher.

The Commission takes account of this difference, to ensure that States with a large Indigenous population have the fiscal capacity to provide the same standard of service to their population as States with small Indigenous populations. However, just as it acknowledges that Indigenous and non-Indigenous people use services at different levels, it also acknowledges that different groups of Indigenous people use services at different levels.

According to the 2016 Census, 20% of Australia's Indigenous population live in the most disadvantaged Indigenous areas, where 48% of Indigenous households have insufficient bedrooms, and only 27% of Indigenous adults are employed. These areas are predominantly remote (71% live in remote areas). Because of the high levels of disadvantage and the costs of providing services in remote areas, States spend $26 000 per Indigenous person in this group.

20% of Australia's Indigenous population live in the least disadvantaged Indigenous areas, where 11% of Indigenous households have insufficient bedrooms, and 55% of Indigenous adults are employed. These areas are predominantly urban (81% live in major cities). While many individuals within this group may not be disadvantaged, this group is on average still among the most disadvantaged in the broader Australian population, and States spend $13 800 per Indigenous person in this group.

Estimates of Australia's Indigenous population change as people change whether they identify as Indigenous in the Census. Between 2011 and 2016, the Indigenous population grew by about 7% more than can be explained by births, deaths and interstate migration. This growth reflects an increased propensity of people to identify as Indigenous. This growth in identification was primarily in the less disadvantaged areas of the country.

Some commentators have expressed concern that increased Indigenous identification in the south-eastern States leads to a redistribution of GST from States with a high proportion of Indigenous people in remote communities towards States with a high proportion of Indigenous people in major cities. However, the Commission identifies total State spending on the most disadvantaged Indigenous people and allocates it between the States in proportion to their shares of the most disadvantaged Indigenous population. Therefore, the increase in Indigenous identification in the less disadvantaged areas has no effect on the allocation of spending on the most disadvantaged Indigenous population.

CHANGES IN STATE CIRCUMSTANCES SINCE THE 2017 UPDATE

1.10 This section describes the main changes in circumstances since the 2017 Update — that is, the changes which occur when revised 2013-14 data are removed and replaced with 2016-17 data. Table 1-4 shows the effect of these changes across the different assessment areas.

Table 1-4 Composition of changes in State circumstances since the 2017 Update

	NSW	Vic	Qld	WA	SA	Tas	ACT	NT	Redist
	$m	$m	$m	$m	$m	$m	$m	$m	$m
Expense requirement	404	205	-494	-97	50	-17	15	-65	673
Investment requirement	261	213	-147	-233	-51	13	11	-66	497
Net borrowing	-19	-15	5	28	2	-3	0	3	37
Revenue capacity	-1 014	-351	-262	1 543	139	-28	-33	6	1 688
Commonwealth payments	-67	467	-289	12	-52	-11	17	-76	496
Total	-435	518	-1 187	1 252	87	-45	9	-199	1 866

Note: The amounts shown in this table are the changes in the GST distribution from replacing revised 2013-14 data with 2016-17 data. They differ from the amounts shown in Table 3 in the Overview, which also include the effects of revising data. Totals may not add due to rounding.

Source: Commission calculation.

1.11 The changes shown in Table 1-4 can be further disaggregated. Table 1-5 shows the changes in individual drivers that made the largest contribution to the changes in State circumstances between the 2017 and 2018 Updates.

Table 1-5 Contribution to changes in State circumstances, 2018-19

	NSW	Vic	Qld	WA	SA	Tas	ACT	NT	Redist
	$m	$m	$m	$m	$m	$m	$m	$m	$m
Mining production	-218	-123	-434	772	32	-17	-8	-3	804
Natural disaster relief	354	90	-555	58	40	17	8	-11	566
Property sales	-348	-142	-25	456	49	0	-13	23	529
Commonwealth payments	-67	467	-289	12	-52	-11	17	-76	496
Taxable payrolls	-180	-78	100	176	19	-12	-13	-12	295
Taxable land values	-212	-16	75	108	33	7	6	1	229
Population growth	118	85	-46	-123	-29	19	0	-24	222
Other causes of change	119	235	-12	-208	-4	-47	13	-97	368
Total	-435	518	-1 187	1 252	87	-45	9	-199	1 866

Note: The amounts shown in this table are the changes in the GST distribution resulting from replacing revised 2013-14 data with 2016-17 data. They differ from the amounts shown in Table 4 in the Overview, which include the effect of revising data. Totals may not add due to rounding.

Source: Commission calculation.

1.12 The following sections explain the main causes of change in State circumstances.

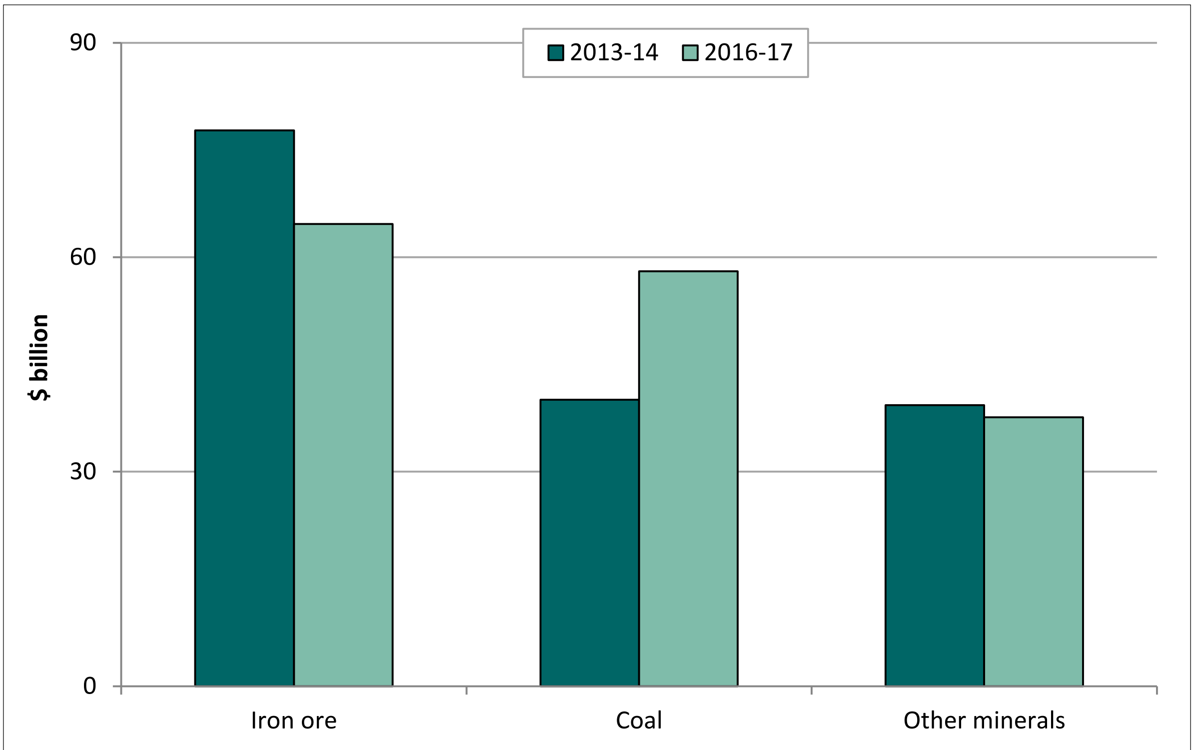
Revenue

Mining production

1.13 Due to the uneven distribution of resource endowments and hence mining activity between States and the large movements in the value of mining production that can occur from year to year, the mining revenue assessment typically produces significant redistributions in GST revenue. Compared with the 2017 Update, $772 million has been redistributed to Western Australia as a result of changes in circumstances.

1.14 Figure 1-1 shows the value of iron ore production decreased between 2013-14 and 2016-17. While there were increases in iron ore production volumes, those increases were more than offset by lower commodity prices. Western Australia's share of North West Shelf royalties also decreased between 2013-14 and 2016-17. Together, these changes reduced Western Australia's fiscal capacity and increased its GST share.

Figure 1-1 Mining value of production, selected minerals, 2013-14 and 2016-17



Source: State data returns.

1.15 ***Iron ore.*** Between 2013-14 and 2016-17 the value of iron ore production in Australia decreased by 17% to $65 billion. Department of Industry, Innovation and Science (Industry Department) data indicate production increased by 26% over this period but was more than offset by reductions in the Australian dollar price of iron ore. As Western Australia accounts for around 98% of the value of Australia's iron ore production, the fall in the value of production affected its fiscal capacity most.

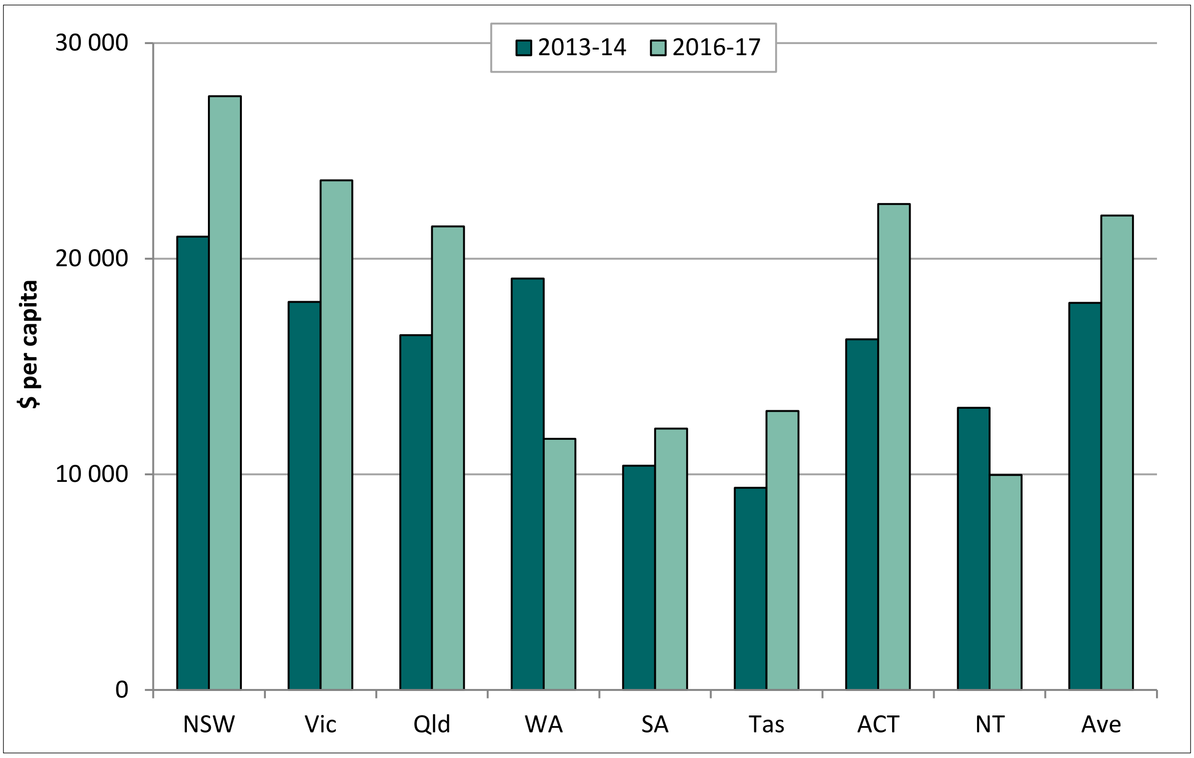
1.16 ***Metallurgical coal.*** Between 2013-14 and 2016-17 the value of coal production in Australia increased by 45% to $58 billion. Industry Department data indicate production grew slowly (4%) over this period and the Australian dollar price of coal increased. As Queensland accounts for more than 60% of the value of Australia's coal production, the increase in the value of production affected its fiscal capacity most.

Property sales

1.17 Stamp duties raised from the transfer of property are volatile. Cycles in property markets can lead to substantial changes across years and States, which can have marked effects on State revenue capacities. The current update has been no exception.

1.18 Between 2013-14 and 2016-17, most States experienced more than 20% growth in the value of property transferred. Three States experienced growth that was less than the average — Western Australia (-38%), South Australia (19%) and the Northern Territory (-23%). As a result, $529 million has been redistributed to these three States, primarily from New South Wales and Victoria. Figure 1-2 shows the change in States' per capita value of property transferred between 2013-14 and 2016-17.

Figure 1-2 Conveyance transactions by State, 2013-14 and 2016-17



Note: Data are adjusted to account for differences between States in the scope of conveyances.
Source: State data returns.

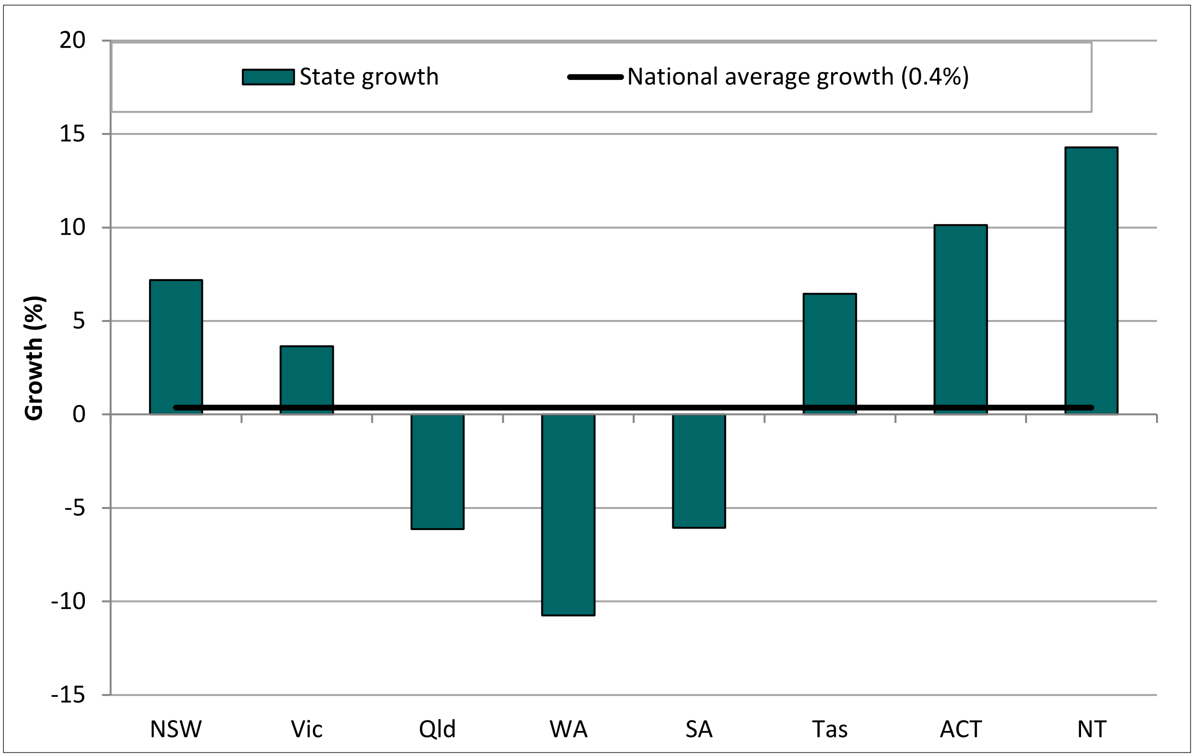
Taxable payrolls

1.19 Changes in State capacities to raise payroll tax redistributed $295 million in GST revenue. The redistribution was driven by differences across States in the rate of growth of taxable payrolls between 2013-14 and 2016-17. These differences are shown in Figure 1-3.

1.20 The Commission uses CoE data to measure States' payroll tax bases. National average growth in taxable CoE between 2013-14 and 2016-17 was 0.4%. New South Wales, Victoria, Tasmania, the ACT and the Northern Territory had above average growth in taxable CoE over the period, increasing their capacities to raise payroll tax and reducing their GST shares.

1.21 Taxable CoE fell in Queensland, Western Australia and South Australia between 2013-14 and 2016-17, resulting in a significant reduction in their ability to raise payroll tax and an increase in their GST shares. While CoE in Queensland and South Australia has increased slightly since 2013-14, the proportion that is taxable has fallen in both States, so that they are assessed as being able to raise lower levels of payroll tax. Western Australia's CoE has fallen every year since 2014-15, with the decline resulting in its 2016-17 CoE being 4.8% lower than the level in 2013-14.

Figure 1-3 Growth in per capita taxable CoE, 2013-14 to 2016-17



Source: Commission calculation.

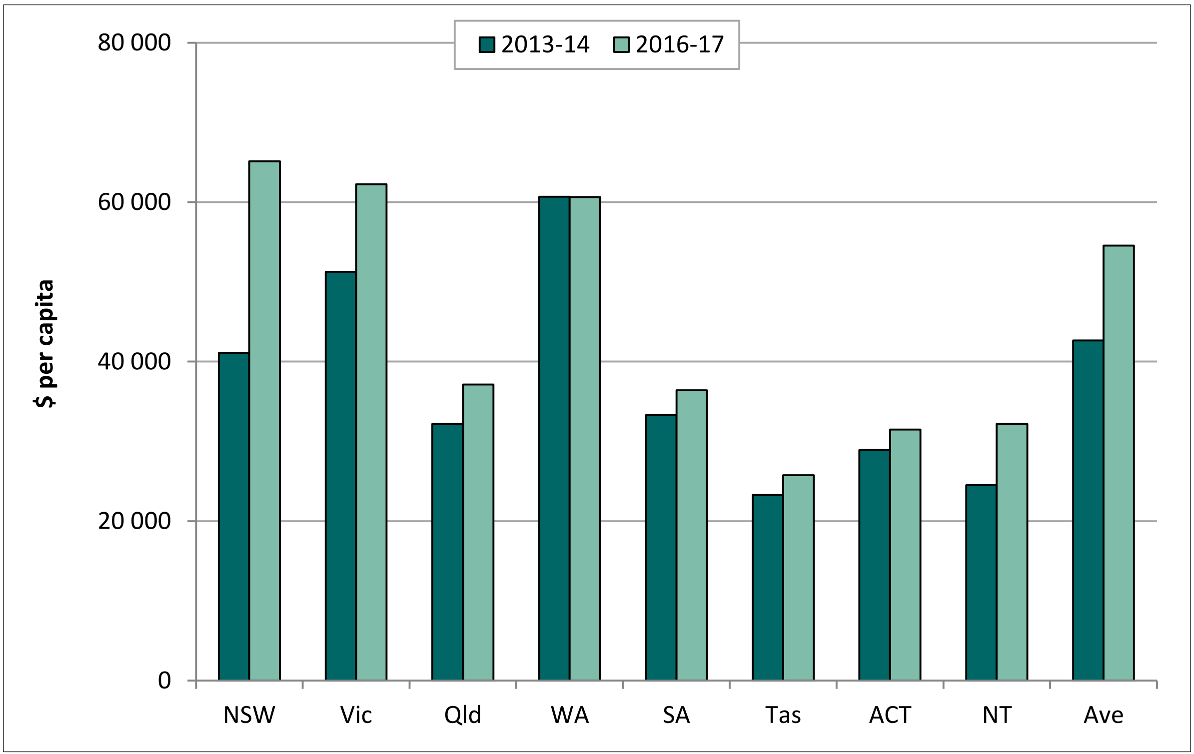
Taxable land values

1.22 Property market cycles can lead to year on year changes in State land values. These cycles have changed State land tax capacities in this update.

1.23 Between 2013-14 and 2016-17, all States experienced growth in the value of their taxable land. Only New South Wales (66%) experienced growth in excess of the average (34%). As a result, the fiscal capacity of New South Wales has risen relative to other States and its GST share has reduced by $212 million. The growth in taxable land values mirrors growth in total land values. National accounts data show that, between June 2013 and June 2016, State land values increased 34%, with only New South Wales (49%) and Victoria (43%) experiencing above average growth.[3]

1.24 Figure 1-4 shows the change in States' per capita taxable land values between 2013-14 and 2016-17.

Figure 1-4 Total taxable land values by State, 2013-14 and 2016-17



Source: State data returns.

Commonwealth payments

1.25 As well as the GST, the Commonwealth makes other payments to the States for specific purposes (PSPs). Equalising the fiscal capacity of the States to provide services requires the Commission to take account of the total expenditure each State would incur to provide the average level of services and the revenue they have available to finance it. This includes the revenue they can collect from their own tax bases under average policies and, consistent with the terms of reference, the revenue

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3 ABS, *Australian System of National Accounts*, 2015-16, Cat. No. 5204.0, Table 61.

they receive through PSPs.[4] To the extent that a State receives above average per capita amounts of PSPs, less GST is required to equalise its fiscal capacity. Conversely, if a State receives below average amounts of PSPs, it requires more GST.

1.26 Between 2013-14 and 2016-17, there were changes in the amounts paid and the interstate distribution of some PSPs, particularly payments for road and rail infrastructure, National Health Reform and Students First government education funding, which had repercussions for the GST distribution.

1.27 Victoria's share of payments was lower in 2016-17, increasing its GST share. This was mainly due to a reduction in its share of infrastructure payments for road and rail. In particular, its 2016-17 payment for road infrastructure included a negative adjustment to recoup prepayment of over $300 million for the East West Link project which did not go ahead. Its reduced share of the National Health Reform funding and the use of 2016 Census based data in this update also contributed to its higher GST share.

1.28 Queensland's share of payments was higher in 2016-17, reducing its GST share. This was mainly due to large payments for road and rail infrastructure, such as for works on the Toowoomba Second Range Crossing and Gateway Upgrade North, and the construction of the Moreton Bay Rail Link. Its higher share of the National Health Reform funding also contributed to its reduced GST share.

1.29 Western Australia's share of payments was slightly higher in 2016-17, reducing its GST share. Its higher share of National Health Reform funding and the use of 2016 Census based data contributed to the change. This was nearly offset by its reduced share, and the cessation of backcasting, of the Students First funding, and its reduced share of payments for Remote Indigenous Housing.

1.30 South Australia's share of payments was higher in 2016-17, mainly due to large payments for the construction of the Northern Connector and North-South Corridor.

1.31 Tasmania's share of payments was higher in 2016-17, mainly due to the cessation of backcasting of the Students First funding and large payments for construction works on the Midland Highway in 2016-17.

1.32 The Northern Territory's share of payments was higher in 2016-17 due to its increased share of funding for National Health Reform and Students First, and payments under the Health and Hospital Fund and Remote Indigenous Housing.

1.33 New South Wales' share increased slightly across a range of payments, decreasing its GST share, while the ACT's share fell slightly across a range of payments, increasing its GST share.

4 The Commission excludes revenue received through PSPs under certain circumstances, including when directed to do so by the terms of reference. Commonwealth payments that have no impact on the relativities are discussed in Chapter 2.

1.34 The main payments causing changes in the GST distribution in this update are shown in Table 1-6.

Table 1-6 Changes in GST distribution due to changes in Commonwealth payments, 2018 Update

	NSW	Vic	Qld	WA	SA	Tas	ACT	NT	Redist
	$m	$m	$m	$m	$m	$m	$m	$m	$m
Road infrastructure	-82	307	-122	-19	-79	-18	9	4	319
Rail infrastructure	-6	129	-78	-19	-17	-3	-4	-2	129
National health reform	40	23	-32	-36	18	-1	12	-24	93
Students First funding (a)	12	13	-42	22	18	-3	4	-24	69
Remote Indigenous housing	-18	-26	21	40	2	-2	-2	-14	62
Other	-13	20	-36	24	6	17	-1	-16	67
Total	-67	467	-289	12	-52	-11	17	-76	496

(a) Government schools component.
Source: Commission calculation.

1.35 More information on the changes arising from the assessment of individual Commonwealth payments is in the supporting information for this update available on the Commission's website (https://cgc.gov.au/).

Expenditure

Natural disaster relief

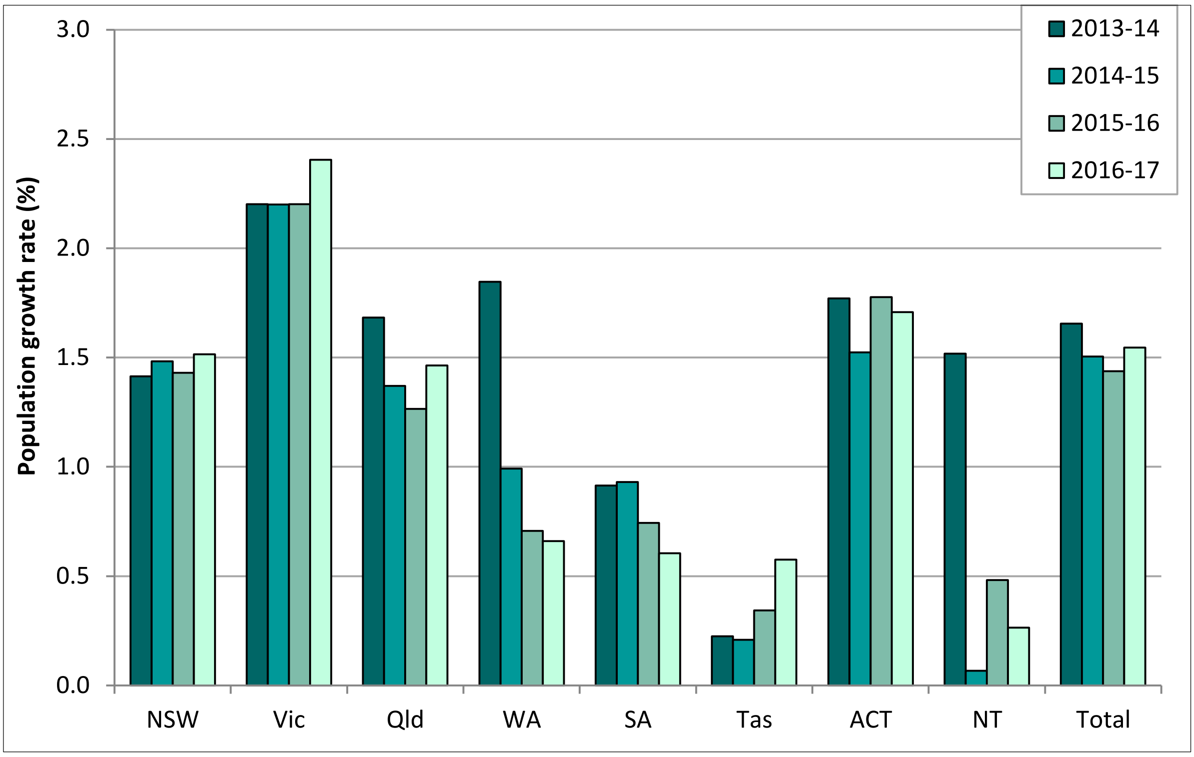
1.36 Queensland's natural disaster relief expenses (net of Commonwealth assistance) were lower in 2016-17 compared to 2013-14, reflecting fewer major disasters in the latter period. This reduced Queensland's GST share, thereby increasing the GST shares of the other States. The increase in GST for the Northern Territory was more than offset by upward revisions to its Natural Disaster Relief and Recovery Arrangements (NDRRA) revenue from the Commonwealth for 2014-15 and 2015-16.

Population growth

1.37 Over the past four years, Australia's population growth has remained around 1.5% per year.[5] However, State population growth rates have varied considerably. Figure 1-5 shows that growth increased in New South Wales, Victoria and Tasmania between 2013-14 and 2016-17, leading to a significant increase in their assessed needs for capital investment.

[5] As measured by births, deaths and net migration.

Figure 1-5 Population growth, 2013-14 to 2016-17



Source: ABS, *Australian Demographic Statistics*, Cat. No. 3101.0.

1.38 Victoria's population growth of 147 000 people in 2016-17 was the greatest increase in population of any State on record. Due to its above average share of national population growth, it now receives an additional $85 million more than an EPC share of GST for its infrastructure needs.

1.39 Queensland, Western Australia, South Australia and the Northern Territory had slowing population growth between 2013-14 and 2016-17, reducing their need for GST.

1.40 Western Australia's population growth has fallen from well above average to well below. Western Australia's population growth in 2016-17 was 37% of the level it had been four years earlier, and one quarter of its peak population growth in 2012-13. For the first time since population growth became a driver of the GST distribution in 2010-11, population growth will lead to a redistribution of GST away from Western Australia.

1.41 The Northern Territory's population growth was around average in 2013-14. Since then it has, on average, been the slowest in the nation. This has led to a significant reduction in the Northern Territory's need for investment. However, given the high level of infrastructure assessed for each Territorian, even with its slow population growth, the Northern Territory still receives above an EPC share of GST.

WHY STATE FISCAL CAPACITIES DIFFER

1.42 Differences among the States in economic, social and demographic characteristics affect their expenditures and revenues, and contribute to differences in GST distributions. Table 1-7 shows how these differences contribute to differences in the recommended GST distribution.

Table 1-7 Difference from an equal per capita distribution of GST, 2018-19

	NSW	Vic	Qld	WA	SA	Tas	ACT	NT	Redist
	$m	$m	$m	$m	$m	$m	$m	$m	$m
Expense requirement	-2 428	-4 972	1 605	2 324	472	537	-194	2 657	7 594
Investment requirement	333	1 254	-426	-485	-332	-159	-20	-165	1 587
Net borrowing	8	-182	27	70	47	22	-3	11	185
Revenue raising capacity	-956	2 882	583	-5 531	1 932	717	332	40	6 487
Commonwealth payments (a)	22	817	-505	5	69	-58	85	-434	997
Total difference from EPC	-3 021	-201	1 284	-3 618	2 188	1 059	200	2 109	6 840

(a) Includes the impact on the revenue side only. The impact on the expense side is incorporated in the expense requirement line.

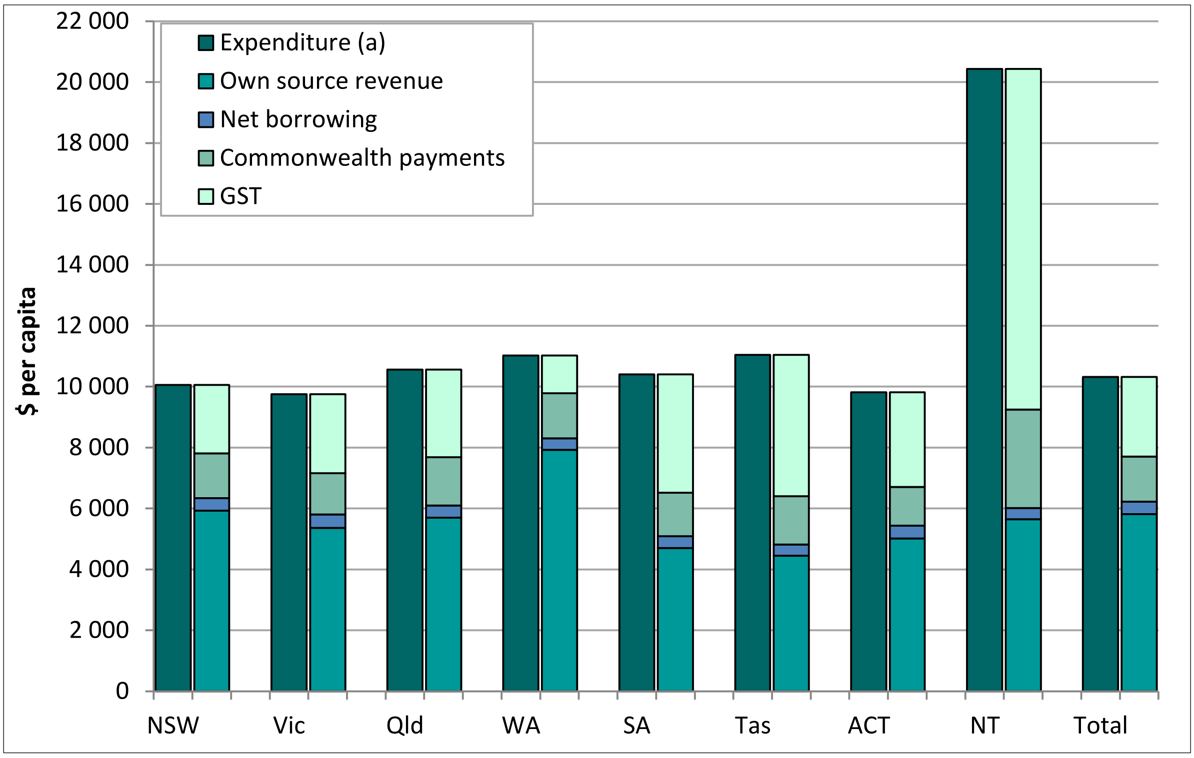
Source: Commission calculation.

1.43 Western Australia's above average revenue raising capacity drives its fiscal strength, despite its higher than average costs of providing services and infrastructure. Its fiscal strength leads to it needing considerably less than its population share of GST. The below average cost of providing services in New South Wales and Victoria is the main reason for their fiscal strength, although this is mitigated somewhat for Victoria by its below average strength in revenue raising. The relatively low fiscal capacities of South Australia, Tasmania and the ACT stem mostly from below average capacities to raise revenue, while Queensland and the Northern Territory face high costs of providing services.

1.44 Figure 1-6 shows this from a slightly different perspective. In the figure, the per capita GST requirement for each State is shown as the difference between a State's total assessed expenditure (expenses and investment) and the sum of its assessed own source revenue, net borrowing and Commonwealth payments. While Western Australia has the third highest assessed expenditure (expenses plus capital expenditure) per capita, this is almost covered by its very high capacity to raise revenue. This leaves a relatively small requirement for GST revenue to give it the capacity to deliver an average standard of service.

1.45 The Northern Territory has such a high cost of delivering services that even with its significantly higher than population share of Commonwealth payments and only slightly below average capacity to raise revenue, it still requires a very large share of the GST to have the capacity to deliver an average standard of service.

Figure 1-6 Illustrative assessed budgets per capita, 2018-19



(a) Includes expenses and investment.
Source: Commission calculation.

1.46 The main economic and demographic factors causing differences in State fiscal capacities are shown in Table 1-8. It shows, for example, that Victoria needs an additional $2 810 million in GST above an EPC share to recognise its below average capacity to raise revenue from mining, while Western Australia needs $4 927 million less than its EPC share because of its very high capacity to raise mining revenue.

1.47 In this update, the Commission again observes significant differences in the innate fiscal capacities of States, which warrant a distribution of GST revenue that differs significantly from one based on State population shares. Further information on why State fiscal capacities differ is provided in Chapter 3, Volume 1 of the 2015 Review report.

Table 1-8 Drivers of difference from an equal per capita distribution of GST, 2018-19

	NSW	Vic	Qld	WA	SA	Tas	ACT	NT	Redist
	$m	$m	$m	$m	$m	$m	$m	$m	$m
Revenue raising capacity									
Mining production	1 977	2 810	-658	-4 927	486	178	188	-54	5 639
Property sales	-2 141	-242	442	793	760	240	38	109	2 383
Taxable payrolls	-536	423	478	-993	466	200	7	-46	1 575
Taxable land values	-449	-234	406	-173	266	95	64	25	857
Other revenue	193	124	-85	-231	-46	3	35	6	362
Total revenue	-956	2 882	583	-5 531	1 932	717	332	40	6 487
Expenditure requirements									
Socio-demographic characteristics									
Remoteness and regional costs	-1 172	-952	709	373	87	394	-142	703	2 266
Indigenous status	9	-1 583	698	198	-129	107	-65	765	1 777
Socio-economic status	98	-108	81	-178	404	55	-230	-122	638
Other SDC (a)	-34	-751	365	86	147	42	4	141	785
Total	-1 099	-3 393	1 853	478	509	599	-433	1 487	4 925
Wage costs	157	-390	-228	712	-242	-188	100	79	1 048
Urban centre size	258	700	-495	22	-112	-216	-50	-107	980
Administrative scale	-448	-301	-171	46	126	236	243	268	920
Population growth	-46	674	-79	-297	-172	-86	-29	35	710
Small communities	-272	-249	88	160	62	22	-17	206	538
Economic activity	-178	-133	75	178	64	17	-49	26	360
Road length	-144	-168	76	140	41	-8	-16	80	336
Other expenses	-316	-640	87	468	-88	25	35	428	1 043
Total expense and investment (b)	-2 088	-3 900	1 206	1 908	187	400	-216	2 503	6 204
Commonwealth payments	22	817	-505	5	69	-58	85	-434	997
TOTAL	-3 021	-201	1 284	-3 618	2 188	1 059	200	2 109	6 840

Note: For explanations of what each effect includes see the supporting information to this report located on the Commission's website (https://cgc.gov.au/).
(a) Other SDC refers to other socio-demographic composition.
(b) This includes the impact of net borrowing.
Source: Commission calculation.

SIZE OF THE EQUALISATION TASK

1.48 States have different fiscal capacities at the beginning of the equalisation process. The distribution of GST revenue both increases and equalises those capacities. The size of the equalisation task is determined by the variation in their initial fiscal capacities. As they diverge, more GST is required to achieve equalisation.

1.49 The process of distributing GST revenue can be thought of in either of two ways.

- GST revenue is first distributed on a population basis, raising the fiscal capacity of all States equally. Then there is a redistribution to achieve equalisation –

from States with above average capacity to those with below average capacity. The size of this redistribution is one measure of the equalisation task.

- GST revenue is first distributed to bring the initial fiscal capacities of all States to that of the strongest. The remaining GST is then distributed equally among all States. The GST required to achieve the first step is an alternative measure of the equalisation task.

1.50 These two measures, which can be expressed in dollars or as a proportion of GST revenue, highlight different aspects of the equalisation task. The first identifies the aggregate transfer from an EPC distribution for States with above average fiscal capacities to States with below average fiscal capacities. The second identifies the difference between the strongest State and the average of the others. Taken together they illustrate how the equalisation task is evolving.

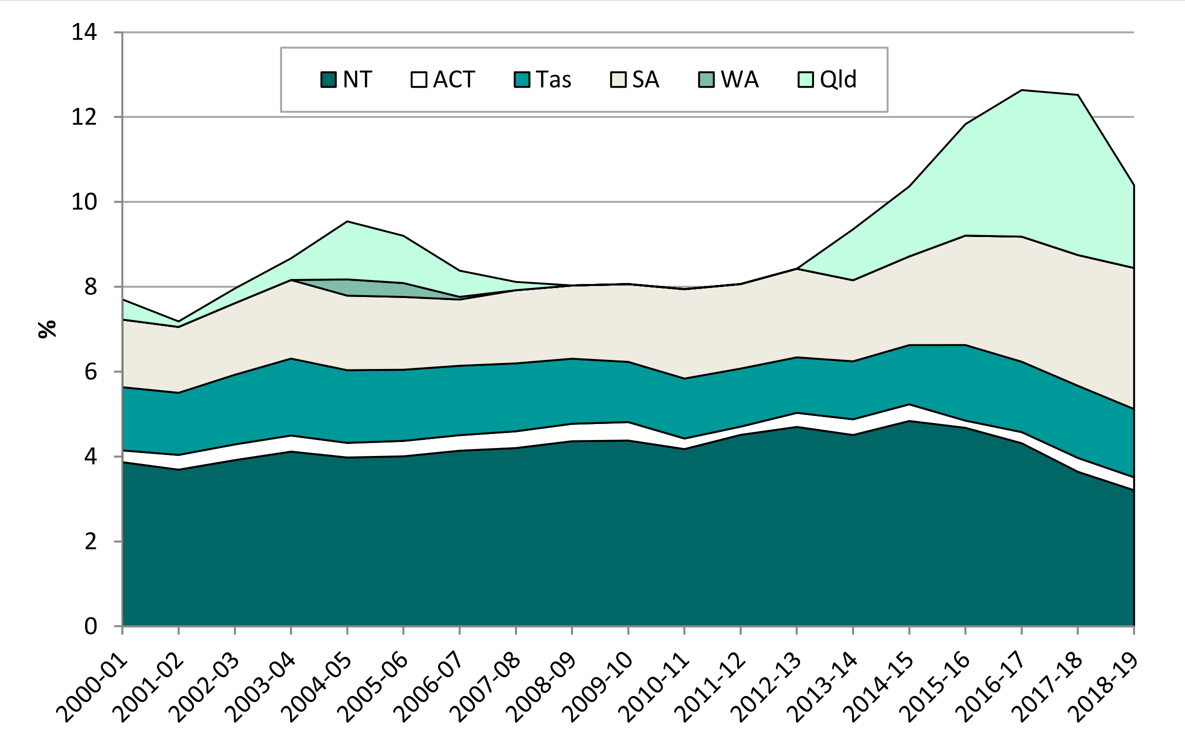
1.51 Note, however, that these are conceptual illustrations of equalisation only and do not reflect what the Commission does in practice. For example, to take the second approach described above, the Commission's objective is not in fact to 'level up' seven States to the fiscal capacity of the fiscally strongest State; rather, it seeks to ensure that every State, including the fiscally strongest, has the same capacity to provide the average standard of State services.

1.52 In relation to the first measure, Figure 1-7 shows that the proportion of GST redistributed to the States with below average fiscal capacities increased between 2010-11 and 2016-17, mainly due to the deterioration in Queensland's assessed fiscal capacity. Since that time, the proportion has decreased. In this update, 10.4% of the GST pool is redistributed to the four less populous States and Queensland to achieve fiscal equalisation, down from 12.5% in last year's update.

1.53 In this update, the redistribution in 2018-19 to the four less populous States accounts for 81% of the $6.8 billion GST redistribution shown in Figure 1-7. These States have about 11.7% of Australia's population and receive 20.1% of the GST, which is similar to the long-term average proportion of 20.4%. Redistribution to these States is mostly the result of weaker revenue bases and higher service delivery costs.

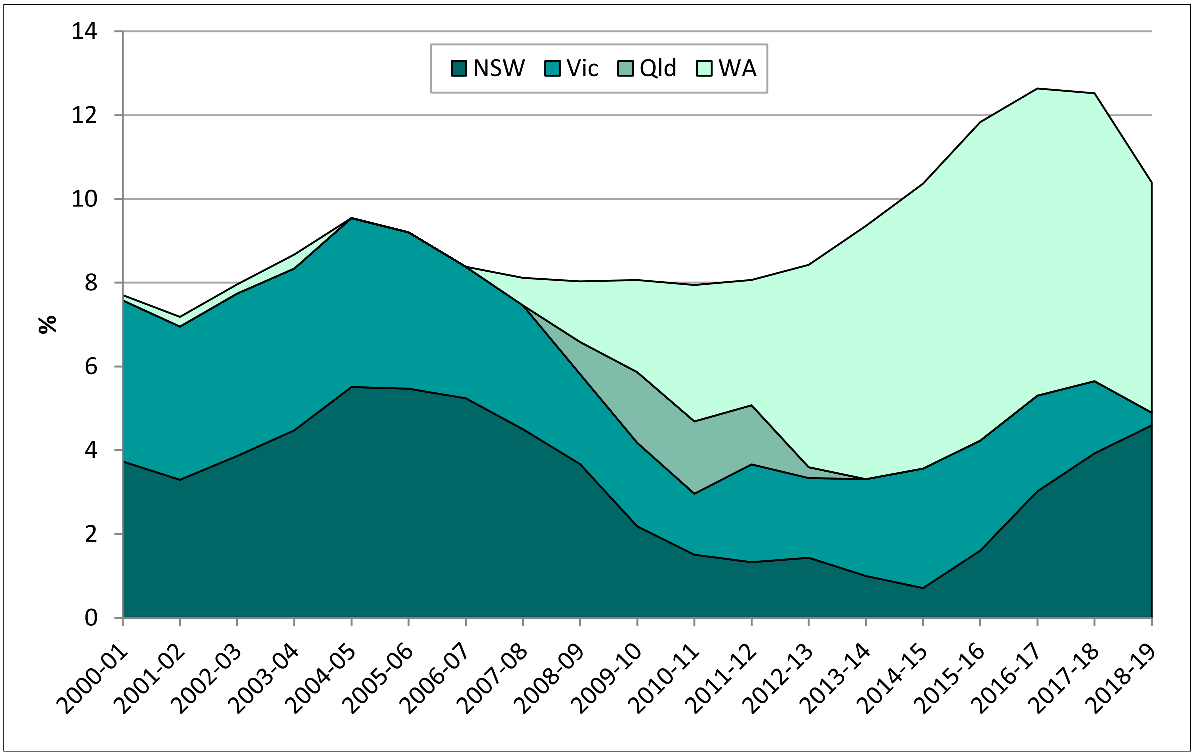
1.54 Figure 1-8 shows the contribution of States with above average fiscal capacities to the GST redistribution. Western Australia's assessed fiscal capacity fell in this update for a third year in a row, after nine years of continuous increase. In contrast, this is the fourth consecutive year in which Victoria's fiscal capacity has fallen. Correspondingly, the redistribution from Victoria to the fiscally weaker States has fallen from 2.9% of the GST pool in 2014-15 to 0.3% of the pool in this update.

Figure 1-7 Proportion of the GST redistributed to States with below average fiscal capacities, 2000-01 to 2018-19



Source: Commission calculation.

Figure 1-8 Proportion of the GST redistributed from States with above average fiscal capacities, 2000-01 to 2018-19



Source: Commission calculation.

1.55 Considering the second measure of the equalisation task reveals a different aspect of the equalisation task. Table 1-9 shows the size of the equalisation requirement in 2018-19. All States except Western Australia require different per capita amounts of GST to achieve the same fiscal capacity as Western Australia, the State with the strongest fiscal capacity. The remainder of the GST revenue is shared equally amongst all States, including Western Australia. In 2018-19, about 53% of the GST revenue was needed for all States to achieve the same fiscal capacity as Western Australia.

Table 1-9 Illustrative distribution of GST, 2018-19

	NSW	Vic	Qld	WA	SA	Tas	ACT	NT	Ave
	$pc	$pc	$pc	$pc	$pc	$pc	$pc	$pc	$pc
Equal per capita	1 242	1 242	1 242	1 242	1 242	1 242	1 242	1 242	1 242
Equalisation requirement	1004	1 349	1 636	0	2 637	3 398	1 859	9 940	1 380
Per capita allocation	2 246	2 591	2 878	1 242	3 879	4 640	3 100	11 181	2 622

Source: Commission calculation.

1.56 This measure of the size of the equalisation task increased rapidly prior to 2017-18. From 2000-01 to 2007-08, it fluctuated between 14% and 17% of GST revenue, as first Victoria and then New South Wales became the fiscally strongest State. In 2008-09, Western Australia became the fiscally strongest State. As Western Australia's fiscal capacity became progressively stronger, this measure of the size of the equalisation task increased from 14% of the pool in 2008-09 to 70% in 2016-17. With the recent decline in Western Australia's fiscal capacity, it has fallen to 66% in 2017-18 and 53% in 2018-19. Where the fiscally strongest State has a relatively small population, it will necessarily mean a large share of the pool is required to achieve equalisation (and vice versa). Population differences between the fiscally strongest and the other States affect the size of the equalisation task.

1.57 Neither measure perfectly captures the totality of how the equalisation task has evolved over time. Taken together they show:

- the equalisation task generated by the less populous States together has been greater in recent years but fell in the two most recent updates
- because Queensland's fiscal capacity fluctuates around the average, it sometimes adds to, and sometimes moderates, the equalisation task
- the task of 'catching up' with Western Australia grew significantly prior to the 2017 Update (reflecting the unprecedented increase in that State's own-source revenues, largely driven by the global commodities boom), but has since been decreasing.

1.58 A time series of per capita relativities since the introduction of the GST in 2000-01 is available in the supporting information for this update on the Commission's website (https://cgc.gov.au/). An overview of Commonwealth-State financial relations in Australia, including a discussion of horizontal and vertical fiscal imbalances, is also available on the Commission's website.

CHAPTER 2

NEW ISSUES IN THIS UPDATE

2.1 In each update, the Commission identifies a range of new issues that might affect the GST distribution. New issues can be grouped into the following types:

- data issues, concerning how the latest available data, or changes to data availability, are incorporated into assessments
- assessment issues, relating to how changed circumstances are incorporated into assessments
- the treatment of Commonwealth payments, including new payments and payments relating to national agreement arrangements
- other issues.

2.2 Before deciding how new issues should be resolved, the Commission consults the States.[1] The issues that arose in this update and the Commission's decisions on them are explained in this chapter. Discussion papers and State submissions can be viewed on the GST Inquiries — 2018 Update page accessed from the Commission's website (https://cgc.gov.au/).

DATA ISSUES

Use of new Census data

2.3 Most data from the 2016 Census are now available and can be used in the 2018 Update, although some data will not be available until later in 2018. The Commission's terms of reference require it 'where possible, [to] use the latest available data'.

2.4 As a result, the Commission has used revised data based on the 2016 Census for:

- total Estimated Resident Population (ERP) levels
- Indigenous populations
- measures of socio-economic status for Indigenous and non-Indigenous populations

1 Commission staff sent two discussion papers on the issues relevant to this update to the States and asked for comments. These papers are referred to as the New issues paper in this chapter.

- discrete Indigenous communities classification
- measures of urban areas
- social housing use.

2.5 As explained below, the Commission has continued to use 2011 based Census data for:

- Indigenous population estimates and the associated socio-economic status in the Justice assessment
- definitions of remoteness
- service delivery scale areas
- measures of local roads in unincorporated areas
- Socio-economic index for areas (SEIFA).

2.6 The Commission has used measures of population growth including intercensal differences, based on the ABS estimates of population levels, in the capital assessments.

2.7 Chapter 1 describes the various effects of the new Census data and associated population estimates on the GST distribution in this update.

Data quality

2.8 The ABS established an independent panel to independently review and assure the quality of statistical outputs from the 2016 Census. The panel concluded that the 2016 Census data are fit-for-purpose and are of comparable quality to the 2011 and 2006 Census data.

2.9 Western Australia and the Northern Territory considered the quality of the 2016 Census is questionable and fit only for some purposes. They argued the Commission should use new data selectively.

2.10 On the basis of the independent panel advice and its own investigations, the Commission considered that data quality does not preclude the use of the 2016 Census data in the 2018 Update, although the fitness for the Commission's purposes of specific datasets needs to be considered on a case by case basis.

Estimated Resident Population (ERP)

2.11 ***Background.*** The ABS's latest estimate of Victoria's population for 30 June 2016 was 111 000 higher than the comparable earlier estimate made without data from the 2016 Census data (2011 Census data adjusted for births, deaths and net migration between 2011 and 2016). For Western Australia, the new estimate was 58 000 lower. The ACT's new estimate was 7 000 higher. No other State had a significant change to their estimates. To produce a consistent time series, the ABS has retained the 2011 population estimate, and added an additional component of population growth to reconcile the 2011 and 2016 level estimates. This additional component, known as intercensal difference, reduced the annual population growth in Western Australia by around 11 000 per year between 2011 and 2016, and increased growth in Victoria by around 21 000 per year. This is the practice the ABS has followed in every Census since ERP was first developed.

2.12 The Commission flagged with States its intention to use the ABS published population series for category assessments and closing populations in the capital assessments. This was on the basis that the ABS has endorsed its published population series as the best measure of **population levels**, and there is no reason to consider that any alternative series better reflects historical population levels.

2.13 States' needs in the capital assessments are driven by **population growth**. To estimate population growth, the Commission was faced with a choice of either using change in population levels between years (which incorporated the intercensal difference component in the ABS estimates of population growth), or ABS estimates of births, deaths and net migration (which do not incorporate any intercensal difference).

2.14 ***ABS views.*** Faced with a similar issue in the 2013 Update, 'the ABS advise[d] that subtracting … components of growth from the preliminary rebased 30 June 2011 ERP [would] provide an effective proxy for a reference point ERP for earlier reference periods'. At that time, the ABS considered that the intercensal difference largely reflected a change in its methods of estimating population between the 2006 and 2011 Censuses. In contrast, following the 2016 Census, the ABS considers that the 2011 and 2016 Censuses are methodologically comparable, although they do contain measurement error. The intercensal difference could reflect errors in one or more of:

- the 2011 levels
- the 2016 levels
- the measures of growth.

2.15 The ABS considers that there is no strong evidence for any particular source of error, and it has followed its usual practice of assigning all the intercensal difference evenly across the intercensal periods. It regards these as the official population estimates, which are fit for purpose.

2.16 ***State views.*** Western Australia considered the quality of the 2016 Census to be questionable, and the ABS approach of applying intercensal difference evenly across each year to be excessively simplistic. As such, it considered using actual data on population growth (rather than a simplistic model of attributing intercensal difference evenly across years) was more appropriate. It also stated that the Commission should use levels as published based on the 2011 Census for years to 2015, and only use the 2016 Census based estimates for 2016.

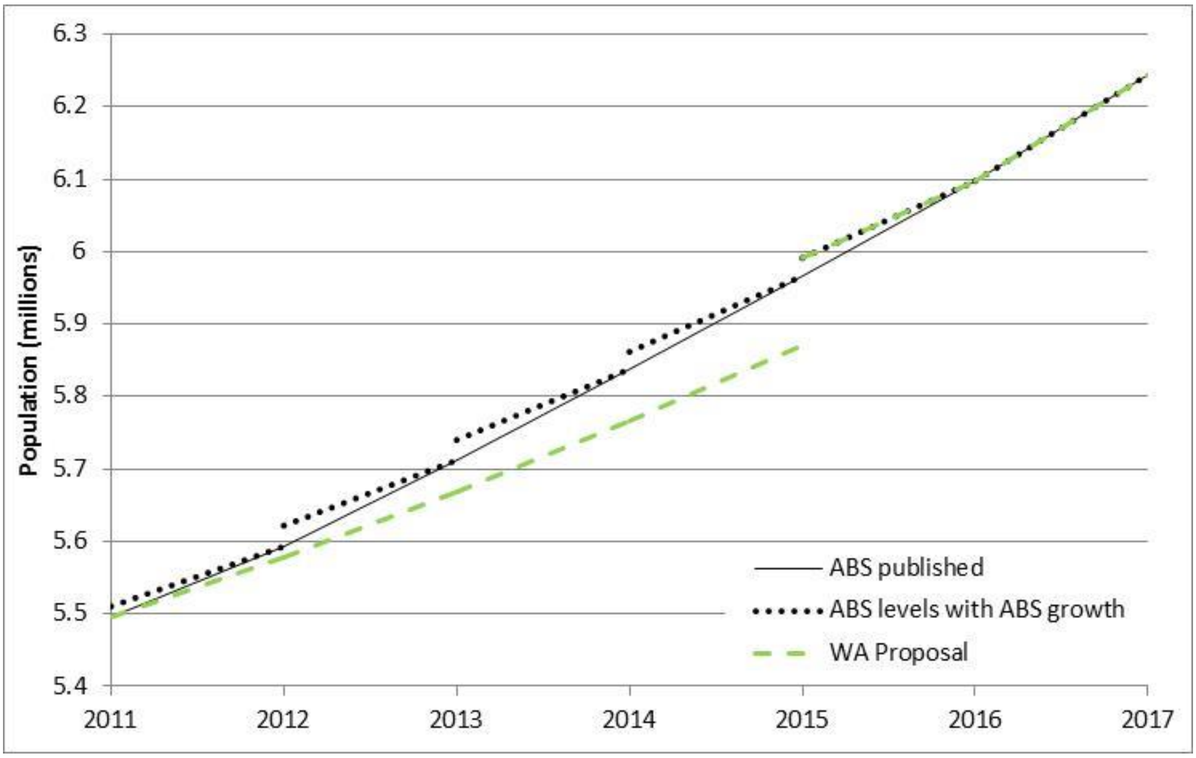
2.17 Tasmania and the Northern Territory considered the Commission should use components of growth to measure population growth. The Northern Territory said that the intercensal difference is not a measure of growth, but rather an error adjustment.

2.18 The other five States considered the Commission should use the published population level series. For Victoria, Queensland and South Australia, this was primarily on the basis that the published series are endorsed by the ABS.

- Queensland noted that this is the ABS usual practice after each Census since 1971. Victoria noted that the ABS measures of jobs growth, using the labour force series, are benchmarked to ABS population estimates, inferring that the ABS considers jobs growth to be best measured by incorporating intercensal difference.
- The ACT argument rested not with the ABS authority but on the premise that, as the Commission is accepting the 2016 level, the appropriate HFE outcome is to accept that Victoria incurred a fiscal cost in providing infrastructure in getting to that level.

2.19 The three alternative approaches are illustrated in Figure 2-1 in respect of Victoria's population.

Figure 2-1 Alternative approaches to measuring Victoria's population



Source: ABS, *Australian Demographic Statistics*, Cat. No. 3101.0.

2.20 ***Commission decision.*** The Commission does not accept the Western Australian argument that using the 2011 Census based estimate of the 2015 ERP represents using the latest available data. While it accepts that this number can be derived from estimates the ABS still endorse (2011 ERP, and growth from 2011 to 2015), a variety of other estimates for those data could also be derived using the latest available data. The latest available estimate for the population level in 2015 is the ABS published number for that series. In the absence of ABS advice or evidence that errors in the 2016 Census are the main source of intercensal difference, the Commission has used 2016 Census data as it is the most reliable, and up-to-date, available data.

2.21 On balance, the Commission has decided to use the ABS data as published, and to use the change in population levels as the official, and most reliable, estimate of growth. The ABS is the subject matter expert in this field and has published data for population estimates that they endorse as fit-for-purpose. The Commission has accepted the ABS advice and practice on use of its data.

2.22 The Commission will consult with States on whether it should more explicitly define its measure of population growth for the capital assessments as part of the 2020 Review.

Indigenous population and socio-economic status

2.23 ***Background.*** The ABS has produced State level estimates of the Indigenous population based on the 2016 Census. These differ from the projections based on the 2011 Census updated for expected births, deaths and net migration. These differences largely reflect that more people identified as Indigenous in the 2016 Census than in the past. These differences, or unexplained growth, are shown in Table 2-1.

Table 2-1 Indigenous population, 2011 and 2016

				Share of Indigenous population		
	2011 based projection	2016 estimate	Unexplained growth	2011 based projection	2016 estimate	Change
	No.	No.	%	%	%	%
NSW	230 564	265 600	15.2	30.9	33.3	2.4
VIC	53 817	57 782	7.4	7.2	7.2	0.0
QLD	213 712	221 398	3.6	28.6	27.7	-0.9
WA	97 907	100 509	2.7	13.1	12.6	-0.5
SA	41 613	42 256	1.5	5.6	5.3	-0.3
TAS	27 114	28 539	5.3	3.6	3.6	-0.1
ACT	7 121	7 524	5.7	1.0	0.9	0.0
NT	74 679	74 509	-0.2	10.0	9.3	-0.7
Total	746 527	798 117	6.9	100.0	100.0	0.0

Source: ABS, *Australian Demographic Statistics*, Cat. No. 3101.0.

2.24 If the newly identifying Indigenous people are less disadvantaged, or less intensively using State services, then the average level of disadvantage in States with high unexplained Indigenous growth would not necessarily increase. The Commission has incorporated the latest population estimates, as well as changes in the attributes of that population. The measures of socio-economic status for the Indigenous (IRSEO) and non-Indigenous (NISEIFA) populations have been updated using the 2016 Census data in a way directly comparable with the measures produced from the 2011 Census.[2]

2.25 The Commission also requires estimates of the Indigenous population for years earlier than 2016-17.

2.26 ***State views.*** States supported the Commission's use of ABS State level estimates of the Indigenous population at June 2016. The Northern Territory recommended that the Commission use growth rates from the 2011 based projections to backcast from the 2016 Census level. Queensland suggested that the Commission linearly interpolate between the 2011 and 2016 estimates. It considered that applying total population growth rates would not reflect the very different demographic features of the Indigenous population, in particular differential growth compared to the non-Indigenous population.

2.27 States were supportive of the Commission's proposed approach to updating the measures of Indigenous socio-economic status (SES) subject to appropriate quality control. However, Queensland considered that an Indigenous specific SEIFA would be preferable to the measure developed for the 2015 Review (IRSEO).

2.28 The Northern Territory recommended using the sub-State 2011 estimates as the basis for the Commission's Indigenous sub-State population estimates as it was concerned about a larger Census undercount in remote areas. Other States supported using the 2016 Census counts.

2.29 ***Commission decision.*** The Commission has estimated the pre-2016 Indigenous populations by applying rates of growth from the 2011 Census based projections to the 2016 Indigenous population estimates. This ensured a consistent approach to population levels and socio-economic profile. A simple linear extrapolation between the 2011 and 2016 Census levels would imply an inconsistent treatment – it would use the 2016 socio-economic profile, while partially incorporating 2011 population levels.

2.30 In the Commission's view, a change from IRSEO to an Indigenous specific SEIFA would represent a method change. It will consider potential improvements to its measure of Indigenous socio-economic status in the 2020 Review.

2.31 The Commission has found that, while there was relatively little bias associated with differential undercount across regions in 2011, Indigenous population growth

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2 IRSEO is the Indigenous Relative Socio-economic Outcomes index. NISEIFA is the Non-Indigenous Socio-economic Index for Areas.

differed much more significantly across regions between 2011 and 2016. Therefore, the Commission has derived sub-State Indigenous population estimates using the 2016 Census counts, scaled to sum to the State total Indigenous and non-Indigenous ERPs and to small area total ERPs. This approach was consistent with the terms of reference requirement to use the latest available data.

2.32 These changes have been incorporated in all assessment calculations where it has been possible to do so. However, in a few cases where administrative data were not available on a consistent basis, or where Census data were not yet available, the Commission has continued to use 2011 Census based data.

2.33 The Justice assessment uses State provided data on offenders and defendants for 2010-11, 2011-12 and 2012-13. Those data were combined with 2011 Census based Indigenous population estimates to calculate Indigenous use rates for the police and courts assessments. While the Commission has data on the distribution of the 2016 Census based Indigenous population, it has no data on their use of justice services. Therefore, it has decided to continue to use the 2011 Census based Indigenous use rates applied to the 2011 Census based Indigenous population distribution.

2.34 For the Health assessment, the Independent Hospital Pricing Authority (IHPA) provided hospital use data for 2016-17 using the 2016 Census based SES profile, but it was unable to provide revised data for the earlier assessment years based on the new profile. The change in Census based classifications affects SES, but not age, Indigeneity or remoteness. Therefore, the Commission has used the 2016-17 data (based on the 2016 SES profile) to apportion the IHPA data for earlier years to SES groups. The Commission considers that, as areas have changed their SES profile between the 2011 and 2016 Census, and the earlier assessment years are closer to the 2016 Census, this approach will better reflect the use of health services by SES. For example, the 2016-17 data indicate that 17% of major city 0-14 year old non-Indigenous admitted patient services were provided to people in high SES areas (as defined in the 2016 Census) while, in 2015-16, using 2011 Census definitions, the proportion was 19%. The Commission has adjusted the 2014-15 and 2015-16 IHPA data so that 17% of major city 0-14 year old non-Indigenous admitted patient services are in the high SES group.

Other Census issues

2.35 The Commission has adopted the 2016 Census based geographic classifications for significant urban areas, urban centres and discrete Indigenous communities. It has continued to use 2011 Census based classifications of remoteness and service delivery scale areas, since the 2016 Census classifications (or the data to support them) were not available in time for the update. Most States supported this approach.

2.36 Similarly, since the ABS has not yet updated the boundaries of remote and very remote regions, the Commission has not updated its measures of the length of local roads in unincorporated areas,[3] or the population it uses in the assessment of utilities subsidies.[4]

2.37 The Commission has used 2016 Census data to update its measures of use of social housing by Indigenous people and people in different household income groups, but it has continued to use 2011 Census based remoteness areas.

2.38 While 2016 Census based measures of SES for the Indigenous (IRSEO) and non-Indigenous (NISEIFA) populations have been adopted, the measures of socio-economic status for the general population (SEIFA) have not yet been updated for the non-State sector adjustment in the Health assessment (this will be updated by the ABS during 2018).

ASSESSMENT ISSUES

Wage costs assessment – Commonwealth Superannuation Scheme adjustment

2.39 The wage costs disability recognises that comparable public sector employees in different States are paid different wages, in large part because of differences in labour markets beyond the control of State governments. The Commission estimates the impact of those differences using an econometric model of the wages paid to private sector employees in each State, controlling for differences in education, industry, experience and other attributes known to affect wage levels. Since 2014-15, the model has used data from the Characteristics of Employment survey (CoES) produced by the ABS.

2.40 Figure 2-2 shows the modelled outcomes for each State for 2013-14 through 2016-17.

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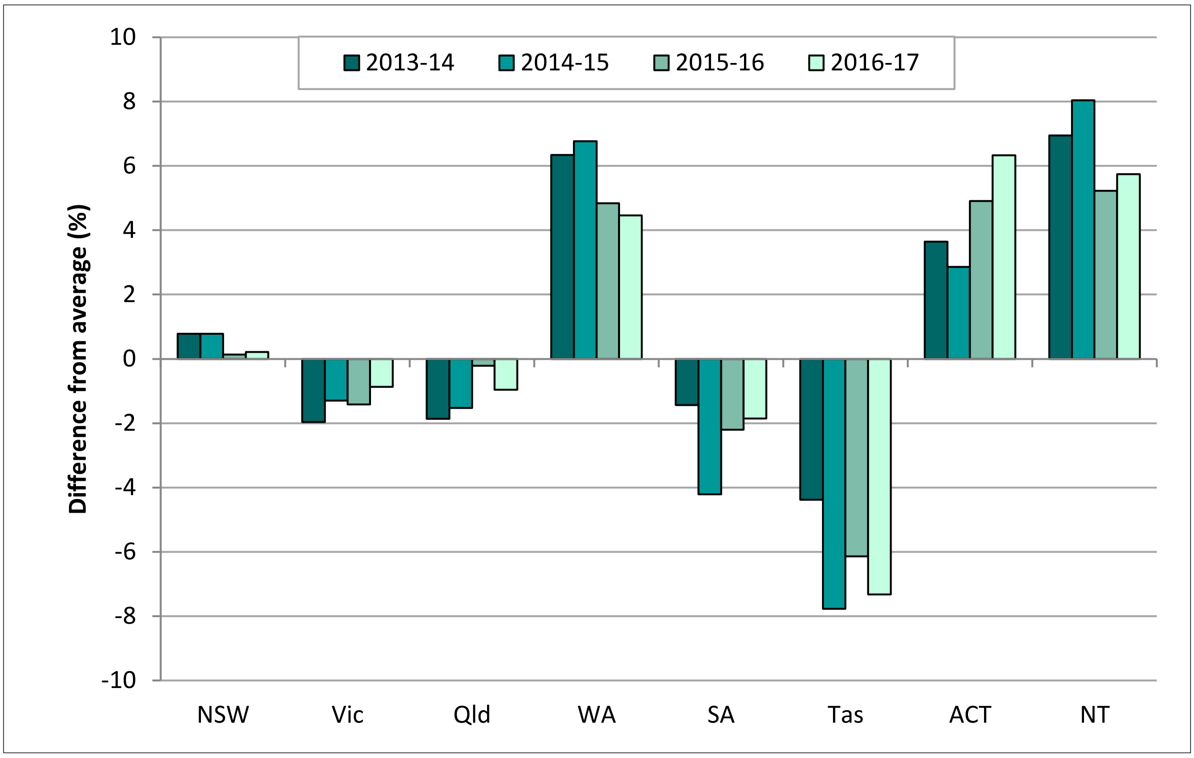
3 The Local roads component of the Roads assessment uses remote and very remote regions with a population density below 0.01 persons per km^2.

4 The utilities subsidies component of the Services to communities assessment uses the populations of urban areas of 50 to 1000 people in remote or very remote areas.

Figure 2-2 Relative wage differentials for 2013-14 to 2016-17



Source: Commission modelling based on ABS Survey of Employment and Training (indexed by the labour price index) for 2013-14 and based on the CoES for later years.

2.41 One issue has arisen in relation to the Wage costs assessment in this update. It is discussed below.

Commonwealth Superannuation Scheme adjustment

2.42 ***Background.*** In the 2017 Update, after consulting the States, the Commission decided to discontinue the adjustment it made to the Wage costs assessment for the ACT and the Northern Territory to account for the higher costs to those States as a result of the Commonwealth Superannuation Scheme (CSS) they inherited at the time of self-government.

2.43 In this update, the ACT provided a submission in support of its view that the CSS adjustment should be reinstated and expanded to include the costs associated with the Public Sector Superannuation Scheme (PSS). The PSS is the other defined benefit scheme that applied to former Commonwealth employees at the time of transition to a separate ACT public service. The Commission last considered the case for a PSS adjustment in the 2004 Review, when it concluded that the costs of the PSS were no greater than average and so no adjustment was merited.

2.44 The ACT submission included data which suggest that the unit cost of the PSS has increased over the past 13 years relative to other State defined benefit superannuation schemes and the superannuation guarantee.[5] It had new data which show that 36% of its public service employees were members of the PSS as at 30 June 2016. It argued that, in light of the new and more reliable data, the Commission should reinstate the CSS adjustment in this update and incorporate the additional costs of the PSS using the same methodology. It said the combined disability would exceed the $30 per capita materiality threshold and that reinstatement of an existing disability, for which there is a conceptual case and established methodology, would not constitute a method change.

2.45 ***State views.*** Most States said that the Commission should not reintroduce the CSS disability, expanded to include the costs of the PSS, in the absence of data that show the adjustment would be material. South Australia said the Commission should apply its supporting principles and exercise its judgment in deciding whether to reinstate the adjustment.

2.46 The Northern Territory supported the ACT proposal to reinstate the expanded CSS disability. It did not support the removal of the adjustment in the 2017 Update on materiality grounds. It added that the previous adjustment only captured expenses related to current employees, whereas the most material costs to it were the ongoing expenses associated with employees accessing the scheme after retirement.

2.47 The ACT considered that the evidence it had provided clearly established that the cost of the PSS had increased to a greater extent than similar schemes in other States. It said that the key issue was the degree of divergence between the costs of the PSS and other schemes, not the reasons for that divergence.[6]

2.48 The ACT also argued that it did not have the choice to close access to the PSS for its new employees prior to the Commonwealth closure of the scheme in 2005. After the enactment of self-government in 1989, its initial employees were transferred from the Australian Public Service and were all members of the CSS. After the closure of the CSS to new members in 1990, all new ACT employees became members of the PSS, with the exception of those transferring from the Commonwealth who were members of CSS.[7] Until the establishment of the ACT Public Service (ACTPS) under its own legislation in 1994, its employees were covered by agreements between the

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5 The ACT data show that the notional employer contribution rate (NECR), the actuarially assessed unit cost, for the PSS increased from 15.4% in 2002-03 to 19.8% in 2016-17. It said that the 2016-17 NECR was 7.51 percentage points higher than a weighted average of defined benefit schemes NECRs in New South Wales and Victoria, and 9.97 percentage points higher than a weighted average of superannuation guarantee rates in six States.

6 It said that the standardised approach taken to the actuarial determination of the cost of government superannuation schemes, reflected in the NECR, meant that NECRs can legitimately be compared across schemes.

7 ACT employees who were CSS members at the time the scheme closed to new members were given the option to remain in the CSS or move to the PSS. That option expired on 30 June 1991.

Commonwealth and the ACT, under which the ACT was not free to alter employment conditions.

2.49 The ACT began to develop alternative superannuation arrangements in November 1997 with a plan to close access to the PSS from 1 July 1999. This plan was abandoned after Commonwealth legislation to close the PSS failed to pass the Parliament, and in response to resistance from trade unions, leading to an Australian Industrial Relations Commission hearing, subsequent to which the ACT agreed with the unions that it would not pursue changes to superannuation benefits before 1 July 2000. The ACT said that from 2000 to 2005 any attempts to change superannuation would have been met with similar resistance and would not have been possible.

2.50 Further, it said that while the PSS was closed to new members from 1 July 2005, as an approved authority under the *Superannuation Act 1990* (Cth), it is required to provide PSS benefits to *existing* members of the PSS who have become members of the ACTPS since 1 July 2005.

2.51 ***Commission decision.*** The Commission has decided, for the reasons outlined below, not to reintroduce the CSS disability, expanded to include the costs of the PSS. In light of the 2004 Review decision not to include a PSS adjustment alongside the CSS adjustment, expanding the CSS adjustment to include the PSS could be construed as a method change. Such a change would be inconsistent with the terms of reference for this update.

2.52 In addition, in the Commission's view, the ACT Government had control over its superannuation arrangements from the establishment of the ACTPS in 1994. It follows that any adjustment would only recognise contributing PSS members who became ACT Government employees prior to that time. Data provided by States suggested that the cost of similar schemes in other States was also high. Together, these suggest that an adjustment would be unlikely to be material.

2.53 Finally, the Commission is inclined to move away from including State-specific adjustments in its expenditure assessments, especially those first introduced to recognise legacy issues affecting newly formed governments for the two self-governing Territories. These Territories have had self-government for well over two decades and much has changed in these jurisdictions over this time. Under these circumstances, the Territories could be expected to have matured sufficiently to be able to deal with historical happenstance, just as all other State governments have been expected to address their legacy issues. Past Commissions have noted the impracticality of attempting to disentangle the effects that past expenditures, undertaken in relation to innumerable projects and circumstances across States, may have had on their current relative fiscal capacities. Focusing only on isolated issues in particular States is arguably inconsistent with the treatment of all other activities.

2.54 The Commission does not accept the Northern Territory's argument that the adjustment should apply to all surviving members of the CSS scheme. Its proposal would result in a cash based adjustment, whereas the Commission's assessments are on an accrual basis.

Commonwealth payments for the National Disability Insurance Scheme

2.55 ***Background.*** In 2018-19, New South Wales and South Australia are scheduled to operate under the full scheme conditions of the National Disability Insurance Scheme (NDIS). The full scheme has been implemented in the ACT since 1 July 2017 but the ACT will not be contributing financially on a full scheme funding basis until 2019-20. Western Australia will be at full scheme in 2020-21. The other States are scheduled to be at full scheme in 2019-20.

2.56 As a consequence of entering the full scheme, New South Wales' and South Australia's National Disability Specific Purpose Payments (SPPs) will cease after 2017-18 (as did the ACT's after 2016-17). These funds are now being paid direct to the National Disability Insurance Agency (NDIA).

2.57 The Commission consulted States on whether to continue the 2015 Review dual assessment approach in this update. The dual assessments of State expenses recognised that, in the transition to full implementation phase of NDIS, States continued to operate the pre-NDIS disability services along with their NDIS contributions.

2.58 The Commission also consulted States on whether it should estimate notional SPPs in the application year for New South Wales, South Australia and the ACT to derive consistent splits of expenses between NDIS and non-NDIS disability services.

2.59 ***State views.*** All States supported the continuation of the 2015 Review dual assessment approach. They also supported the imputation of notional National Disability SPPs for New South Wales, South Australia and the ACT to be used to derive the proportions of NDIS and existing disability services expenses projected for the application year.

2.60 ***Commission decision.*** The Commission has decided to continue the 2015 Review dual assessment approach as the rate at which States move to full scheme is a matter of policy choice and the average policy in the application year is the relevant policy.

2.61 The Commission also decided to impute notional national disability SPPs for New South Wales, South Australia and the ACT to derive the proportions of NDIS and existing disability services expenses projected for the application year. This would ensure that expenses for all States are measured on a consistent basis.

Health assessment

Emergency department data

2.62 ***Background.*** In late 2016, the Commission received advice from the IHPA that the emergency department (ED) data from the National Public Hospital Establishment (PHE) database would not be available from 2014-15. This affected 2014-15 and 2015-16 ED data in the 2017 Update and the Commission had to decide how to deal with the missing activity.

2.63 The ED activity from the PHE database accounted for a small proportion of total ED activity. Most ED activity was being measured through the Non-admitted Patient Emergency Department Care National Minimum Data Set (or EP collection) and Activity-based Funding Emergency Services Care Data Set Specification (or ES collection). Analysis of the 2013-14 ED data for the 2017 Update showed that only about 5% of total ED occasions (or 411 890 occasions) were sourced from the PHE database. However, these occasions were not uniformly distributed across remoteness areas, ranging from 0.1% in major cities to 17.4% in outer regional areas, so ignoring them would disproportionately exclude ED activity in areas outside major cities and have a material effect on the GST distribution.

2.64 After consulting with States during the 2017 Update, the Commission decided to estimate the missing PHE occasions for years after 2013-14 using the number of occasions in 2013-14, rather than the proportion. This was because IHPA advised that improvements to the coverage of EP and ES data collections were likely to measure most of the activity previously captured in the PHE database. Most States supported this approach but suggested that the Commission revisit the issue in the 2018 Update and use hospital level data to assess changes in collection coverage to determine the best approach for estimating the missing PHE activity going forward.

2.65 IHPA has provided the Commission with hospital level data to estimate the ED activity not measured in the two ongoing emergency department data collections (EP and ES). It supplied the following data to facilitate the analysis.

- Data on the number of ED occasions for each hospital in the PHE collection in 2013-14, by hospital remoteness.[8]
- Data on the number of ED occasions for each hospital in the EP and ES collections in 2013-14 and 2014-15, by hospital remoteness.

2.66 Using these data the Commission identified that, of the 163 hospitals that reported their ED occasions in the PHE collection in 2013-14, 100 began reporting in the EP collection in 2014-15,[9] leaving only 63 'non-reporting hospitals'. These 'non-reporting

8 All the hospitals were de-identified and only hospital codes were provided by IHPA.
9 None of the 163 hospitals reported to ES in 2014-15.

hospitals' accounted for 90 850 ED occasions in 2013-14 or 1.2% of total ED occasions in that year.

2.67 The Commission estimated the number and proportion of PHE ED occasions for the 63 'non-reporting hospitals' in 2014-15 by applying a growth factor derived from data for the 100 hospitals that reported in 2013-14 and 2014-15. Using this approach it estimated there would be 88 182 ED occasions for 'non-reporting hospitals' in 2014-15, representing 1.1% of total ED occasions in that year.

2.68 Table 2-2 shows the calculation steps by hospital remoteness area. Most of the 'non-reporting hospitals' were in inner and outer regional areas and only four were in remote areas.

Table 2-2 Estimation of ED occasions from 'non-reporting hospitals' for 2014-15

	Step (1)	Step (2)	Step (3)	Step (4)	Step (5)
	Non-reporting hospitals in 2014-15 (a)	ED occasions for non-reporting hospitals in 2013-14	Growth in activity for hospitals reported in both years (b)	Estimate of ED occasions from non-reporting hospitals in 2014-15 (2)*[100+(3)]	Proportion of ED occasions from non-reporting hospitals in 2014-15
	No.	No.	%	No.	%
Major cities	0	0	-10.6	0	0.0
Inner regional	30	51 017	-1.7	50 170	2.6
Outer regional	28	37 269	-4.2	35 707	3.3
Remote	4	2 139	-12.1	1 880	0.7
Very remote	0	0	2.8	0	0.0
Unknown	1	425	na	425 (b)	0.5
Total	63	90 850	-4.0	88 182	1.1

(a) All the other PHE hospitals (100 in total) reported ED occasions in the EP collection in 2014-15.
(b) The Commission could not derive a growth factor for the unknown hospital so none was applied.
Source: Commission calculation using a special data request from IHPA.

2.69 Analysis indicated that including an estimate for the missing activity would not materially affect the GST distribution and it would be simpler not to make an adjustment to include the missing data. For this reason, the Commission consulted States on whether to use the IHPA ED activity captured by the EP and ES collections for all assessment years in this update without any adjustment.

2.70 ***State views.*** Seven States supported not making an adjustment for the missing ED activity. Western Australia said IHPA data were not well enough understood to allow it to provide comment on the issue.

2.71 ***Commission decision.*** The Commission has decided not to adjust ED activity data in this update because the number of ED occasions not being captured is negligible and the adjustment is not material for any State.

2.72 The Commission notes that IHPA is continuing to work with State health authorities to improve the coverage for the EP and ES collections (especially the EP collection) and it anticipates further improvements in the coverage of these collections in the future.

Transfer of Mersey Community Hospital from the Commonwealth to Tasmania

2.73 ***Background.*** In 2016-17, Tasmania received $736.6 million from the Australian Government under the National partnership agreement on the transfer of the Mersey Community Hospital. This included $730.4 million for the operating costs of the hospital for 10 years, $3.2 million for the delivery of drug and alcohol residential rehabilitation services at the Missiondale Recovery Centre, and $3 million for the provision of palliative care services by Palliative Care Tasmania and The District Nurses.

2.74 In 2016-17, the Tasmanian Government transferred the amount it received for the operation of the hospital ($730.4 million) to TasCorp. The funds are being held in the Mersey Community Hospital Fund. TasCorp will make annual dividend payments from the fund to the Tasmanian Government, equal to the operating costs of the Mersey Community Hospital, escalating at 3.5% each year until cessation of the fund.

2.75 The terms of reference for this update instruct the Commission to exclude the $730.4 million payment from the calculation of per capita relativities. The terms of reference do not contain any instructions about the treatment of the hospital asset transfer from the Australian Government to Tasmania[10] or ongoing support for the delivery of rehabilitation and palliative care services.

2.76 Usually when a payment is excluded from the calculation of per capita relativities, adjustments are made to State expenses to ensure there are no second round effects on the GST distribution. The arrangements for the $730.4 million payment would require a number of data adjustments until 2026-27 to eliminate all second round effects. We have estimated the materiality of making data adjustments for the next 10 years to remove all second round effects and find they are immaterial.

2.77 ***State views.*** States agreed that the payment of $730.4 million should not affect the relativities as instructed by the terms of reference. States, including Tasmania, agreed that the data adjustments to the 2017-18 to 2026-27 assessment years to eliminate second round effects should not be made because they are immaterial.

2.78 States agreed that the asset transfer and payment for rehabilitation and palliative care services should affect the GST distribution.

10 The transfer of ownership of the Hospital (estimated value of $10 million) is effective from 1 July 2017.

2.79 ***Commission decision.*** The terms of reference for this update instruct the Commission to exclude the $730.4 million payment from the calculation of per capita relativities. Therefore, it has treated this payment so it has no effect on the GST distribution. The Commission will not make ongoing data adjustments for second round effects over the next 10 years because they are not material and it will keep the calculations simpler.

2.80 The terms of reference do not contain any instructions about the treatment of the asset transfer or the payments for the delivery of rehabilitation and palliative care services. The asset transfer, which occurred on 1 July 2017 will be included in Tasmania's net investment expenditure in 2017-18 and assessed in the Investment assessment. The payment for the delivery of rehabilitation and palliative care services has been treated as affecting the relativities in this update because it is for a State function and needs are assessed in the Health category.

Schools assessment and the Commonwealth payment for Quality schools

2.81 ***Background.*** National Education Reform funding was to commence from 1 January 2014, with the Commonwealth's offer to States under the National Education Reform Agreement (NERA) open until 30 June 2013. In this context, the Commission received terms of reference for the 2015 Review requiring it:

- not to unwind the recognition of education disadvantage embedded in the funding arrangements
- to ensure no State or Territory received a windfall gain from non-participation.

2.82 To do this, from the 2015 Review to the 2017 Update, the Commission based its assessments of Commonwealth funded government schools on Department of Education projections of the application year State shares of the Schooling Resource Standard (SRS), and used the Commonwealth's *Mid-year Economic and Fiscal Outlook* estimates of State shares of the application year's Students First (or former NERA) payments to assess the associated revenue.

2.83 A new Quality Schools funding approach commenced on 1 January 2018. It retains a reference to an 'ideal' distribution of funds based on the recognition of educational disadvantage through a new SRS and an actual distribution of Commonwealth funds based on a transition period to reach that ideal.

2.84 Negotiations on the new agreement have not been finalised for 2018 or 2019. This has precluded the Commission from following its previous practice of using the application year distribution of funds in its assessment.

2.85 The newly established National Schools Resourcing board membership was announced on 1 November 2017. This is the body responsible for recommending the

SRS weights. It has not yet recommended the socio-demographic formula to apply in 2019.

2.86 ***State views.*** All commenting States considered that the Quality Schools program was sufficiently NERA-like to mean that the terms of reference continued to apply. However, the ACT considered the Commission should use a regression of the Australian Curriculum and Reporting Authority (ACARA) data to better reflect what States do, rather than using the SRS amounts, to ensure the Commission does not 'unwind the recognition of education disadvantaged embedded in the funding arrangements.'

2.87 States also said that the forecast payments were not reliable as negotiations had not yet finished, and hence the Commission should revert to using the distribution of payments in the assessment years, rather than the application year.

2.88 New South Wales considered that a change in method for assessing expenses is not necessary, and a move away from using application year SRS amounts would unwind the intent of the Commonwealth policy. Other States supported using assessment year SRS amounts, as the application year cannot be relied upon to be final.

2.89 ***Commission decision.*** The Commission has ceased backcasting associated with the schools assessment in this update because of uncertainty. It assessed Commonwealth funded school expenditure using SRS weights and student numbers from the assessment years, and assessed revenue from Commonwealth payments using the share of payments States received in the assessment years.

2.90 The Commission considered using the SRS amounts is both simpler and more consistent with the terms of reference requirement than the ACT suggestion of developing an ACARA regression. The Commission accepted the New South Wales argument that to cease backcasting of the SRS amounts could, to some extent, represent an unwinding of the policy prevailing in the application year. However, as that policy is not yet known, the Commission considered it is more reliable to use the SRS amounts from historical years.

2.91 The Commission notes that the new agreement may also include penalty provisions where States do not maintain prescribed funding growth. No penalties have been included in the assessment years for this update. Any treatment of penalty provisions will be determined in the future, if and when they are applied.

Rescaling in the Investment assessment

2.92 ***Background.*** Following the 2017 Update, the Commission became aware of an issue with rescaling in the Investment assessment. When the Commission multiplies two disabilities, the sum of the States' expenditure is no longer the national total, and so it ‘rescales’ or shares the total expenditure in proportion to the States’ shares of the unscaled expenditure.

2.93 However, in the Investment assessment (due to it being possible for different States to require either positive or negative assessed Investment), this approach can create unintended outcomes to the extent that the effect of disabilities can be exaggerated several fold, or in very extreme cases have a reversed sign.

2.94 To address this problem, the Commission consulted States on whether it should calculate the difference between the assessed change in stock and the unscaled expenses and distribute that EPC. This would reduce the impact of rescaling significantly while still capturing the measured effect of the disability.

2.95 ***State views.*** Five States commented on this issue. Victoria, Queensland, South Australia and Tasmania supported the proposed change to the Investment assessment. The ACT supported the solution, but considered that it should only be implemented in those cases where there is actually a mix of positive and negative values, rather than in all assessments were there is a conceptual possibility of such a mix.

2.96 ***Commission decision.*** The Commission has decided to calculate the difference between the assessed change in stock and the unscaled expenses and distribute this EPC. This can also be described as ceasing rescaling in the Investment assessment, and allocating any gap between total assessed Investment and total actual Investment EPC.

2.97 If the Commission were only to do this where there was actually a mix of positive and negative values, as the ACT proposed, it could end up with a different approach in some assessment years to others within the same assessment. The difference between the ACT proposal and the Commission’s decision is immaterial, but the ACT approach is considerably more complex. As such, the Commission decided to apply the new rescaling approach across the Investment assessments.

Treatment of mining royalties where bans have been introduced

2.98 ***Background.*** In its 2015 Review report, the Commission said it would monitor developments in State mining policies to:

- ensure its mineral by mineral assessment was not influencing State behaviour
- check whether other minerals had become material
- ensure the mining revenue base it observed was consistent with average policy.

2.99 In the 2015 Review, the Commission assessed mining revenue capacity using a mineral by mineral approach. It included Coal Seam Gas (CSG) in the onshore oil and gas component and uranium in the other minerals component. Value of production was used as the capacity measure for both components. States that banned the exploitation of these minerals were, therefore, assessed to have zero revenue capacity as they had zero production.

2.100 Since the Review, a number of States have imposed or reinstated bans on CSG and uranium and these minerals are now banned in a majority of States. Currently, the royalties raised on these minerals are small, so that changing their treatment would not materially change States' GST outcomes.

2.101 The Commission consulted States on whether it should change the treatment of royalties where bans on extraction are in place in most States in this update, taking into account that such a change was unlikely to be material.

2.102 ***State views.*** Most States supported no change to the treatment of CSG and uranium in the 2018 Update. The ACT said that, given the uncertainty of the tax bases in the non-taxing States, the most equitable approach is to assess these minerals equal per capita. Western Australia agreed. It said a moderate general discount would be consistent with the option presented in the paper and would recognise that policy influences were more pervasive than just bans.

2.103 Most States also supported reviewing the treatment of mineral bans as part of the 2020 Review.

2.104 ***Commission decision.*** The Commission has decided not to change the mining assessment in the 2018 Update. It noted that any change, including EPC for CSG and uranium, would not be material.

2.105 The Commission did not accept Western Australia's proposal of a general discount applied to the totality of mining revenue. A low discount (12.5%) would be equivalent to treating about $1 billion of royalty revenue EPC, which was substantially bigger than the revenue raised from banned minerals (around $50 million). A general discount would mean changing the assessment method for reasons other than the issue of banned minerals.

2.106 The Commission also decided it would review the treatment of bans in its 2020 Review. In its position paper on '*The principle of HFE and its implementation*', the Commission said its preliminary view was to assess banned minerals EPC.

TREATMENT OF COMMONWEALTH PAYMENTS

Terms of reference requirements

2.107 The 2018 Update terms of reference require the Commission to prepare its assessments on the basis that the following payments should not directly influence the relativities:

- $730.4 million to Tasmania relating to the transfer of ownership of the Mersey Community Hospital
- $1.42 billion to Victoria relating to the Regional Rail Revival program
- $1.2 billion to Western Australia relating to the re-allocated Perth Freight Link Infrastructure funding.

2.108 Accordingly, the payment to Tasmania (made in 2016-17) has been treated in a way that it does not influence the relativities. The payments to Victoria and Western Australia (not paid in the assessment years of this update) will not influence the relativities when they are paid in the assessment years of future updates.

2.109 In addition, as directed by the 2018 Update terms of reference, the Commission has continued to exclude those payments (full amount or 50% of the amount) quarantined by previous terms of reference.

2.110 As is generally the case, the 2018 Update terms of reference also direct the Commission to prepare assessments on the basis that national partnership facilitation payments and reward payments should not influence the relativities. [11]

2.111 The list of quarantined payments and the amounts relevant to this update are available on the [Commission's website](https://cgc.gov.au/) (https://cgc.gov.au/).[12]

Treatment of new Commonwealth payments

2.112 Apart from payments for which the terms of reference have requested special treatment, all Commonwealth payments which affect State fiscal capacities and for which needs are assessed have an impact on the relativities. This is in accordance with the guideline adopted in the 2015 Review.

2.113 Table 2-3 provides a summary of the treatment the Commission has applied to payments which commenced in 2016-17. The Commission has not backcast any other payments commencing in 2017-18 or 2018-19 because they do not represent a major change in federal financial arrangements.

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11 Clause 6(d) of the terms of reference also says the Commission may determine to treat particular (facilitation) payments differently, reflecting the nature of the payment and the role of State governments in providing particular services.

12 See the *Treatment of Commonwealth payments* document under the 2018 Update/Supporting Information/Supporting Documentation section on the Commission's website.

Table 2-3 Treatment of Commonwealth payments commencing in 2016-17

Payment	$m	Treatment	Reason for 'no impact'
HEALTH			
Mersey Community Hospital			
Hospital transfer	730.4	No impact	2018 Update terms of reference requirement.
Drug and alcohol residential rehabilitation treatment and palliative care services	6.2	Impact	
SKILLS AND WORKFORCE DEVELOPMENT SERVICES			
NSW Infrastructure Skills Centre	1.0	Impact	
COMMUNITY SERVICES			
Family advocacy and support services	4.2	No impact	Needs are not assessed. The Commonwealth purchases the service from States.
Women's safety package — technology trials	0.9	Impact	
INFRASTRUCTURE			
Infrastructure investment program — Developing Northern Australia —Northern Australia roads	12.0	Impact	
ENVIRONMENT			
Water infrastructure development fund — feasibility studies component	12.8	Impact	
OTHER			
Northern Queensland Stadium	10.0	Impact	
Tasmanian tourism growth package	1.1	Impact	
Tourism demand driver infrastructure recovery package	3.5	Impact	

Source: Commonwealth of Australia's *Final Budget Outcome 2016-17* and Commission decisions.

2.114 The following sections explain the treatment of payments where States raised issues.

Developing Northern Australia

2.115 The funding is to provide incentives for private sector investment to improve the road network and transport logistics in Northern Australia. This funding has two components:

- improving cattle supply chains
- Northern Australia Roads.

2.116 The Commission consulted States on whether this payment should affect the relativities, since needs are assessed in Investment.

2.117 ***State views.*** Most States said that this payment should affect the relativities because needs are assessed. Western Australia and the Northern Territory considered this payment should have no impact on relativities because the current roads infrastructure assessment does not recognise needs associated with economic development.

2.118 ***Commission decision.*** The Commission has decided that the Developing Northern Australia payment should affect the relativities because needs are assessed in the roads component of investment assessment.

2.119 Both components under the Developing Northern Australia payment have a strong focus on road infrastructure. While the roads infrastructure assessment does not explicitly capture economic development needs, it does capture the road use associated with vehicles across all roads. Therefore, if there are costs associated with constructing roads due to vehicle use, these needs are captured. Some portion of associated road length is also captured to the extent that the required roads also connect populated areas, and that the assessment of road length is a broad measure of needs. While the smaller cattle supply roads may not be captured in the assessment, analysis in the 2015 Review found it immaterial to do so. The Commission considers the needs are adequately assessed and the payment should have an impact on relativities.

National Housing and Homelessness Agreement

2.120 ***Background.*** The ACT sought the views of the Commission on the treatment of the payments under the National Housing and Homelessness Agreement (NHHA), which is scheduled to commence in 2018-19. The ACT considered the new agreement to be a major change in Commonwealth-State financial arrangements and that backcasting the payments would be the standard approach followed by the Commission.

2.121 The ACT said the NHHA represents a major change because:

- it combines funding from the previous National Affordable Housing Agreement with that from the previous National Partnership Agreement on Homelessness, thus converting the latter into an ongoing rather than time-limited payment
- its provisions are being incorporated in Commonwealth legislation, rather than depending solely on inter-governmental agreements
- it contains provisions for financial penalties or partial funding where certain performance requirements are not met. Previously, such provisions applied to reward-type national partnerships, but had never been applied to specific purpose payments.

2.122 The ACT noted that the treatment of financial penalty provisions is discussed in relation to the Quality Schools payments and expected a similar discussion in relation to the NHHA.

2.123 ***State views.*** No other State considered the NHHA to be a major change in Commonwealth-State financial arrangements.

2.124 ***Commission decision.*** The Commission has not backcast the payments under NHHA because they are not paid as a result of a major change in federal financial arrangements. The quantum and distribution of the payments in 2018-19, as shown in the *Mid-year Economic and Fiscal Outlook 2017-18,* will not be of a different order of magnitude from the previous payments (specific purpose payments for National Affordable Housing and national partnership payments for Homelessness).

2.125 The fact that the homelessness part of the payment will now be on-going and that the provisions of the agreement will be incorporated in Commonwealth legislation are not sufficient reasons for backcasting the payments.

2.126 With regard to financial penalties, the Commission does not have, at this stage, the necessary information to decide how it would treat any affected payments. The Commonwealth is currently negotiating bilateral schedules with each State.

National partnership on remote housing

2.127 ***Background.*** In the 2016 Update, the Commission decided to treat 25% of the payments under the National Partnership Agreement on Remote Indigenous Housing (NPARIH) as not affecting the State GST shares because it considered that part of the funding was to address past under-investment by the Commonwealth in remote Indigenous housing and needs were not assessed.

2.128 The Commission said it would review the treatment of Commonwealth payments for remote Indigenous housing when a replacement program for NPARIH had been negotiated. The Commission expected that the Commonwealth legacy issues would be resolved by 2017-18. In this case any future Commonwealth funding would be treated as having an impact.

2.129 As part of the renegotiations of NPARIH, the Commonwealth commissioned a review to consider the impact of the Commonwealth’s investment in remote housing since 2008 and to provide options for addressing future need. It also put in place the Remote Housing Strategy, which commenced in 2016 as an interim arrangement. The review was to be completed at least 12 months prior to the Strategy’s expiry on 30 June 2018.

2.130 The review report (Remote Housing Review) was released at the end of October 2017. The report concluded that while much has been achieved in the provision of remote Indigenous housing, more needed to be done.

- The report estimates that some 3 000 dwellings are still required to be built to meet current needs to 2018, over half of which are in the Northern Territory.
- The review recommends that the costs of a successor remote Indigenous housing program should be equally shared (50:50) between the Commonwealth and the States.

2.131 The Commission consulted States on whether it should wait for a new remote Indigenous housing agreement to be finalised before considering changes to the assessments since, at this stage, there is insufficient information available on the arrangements for 2018-19.

2.132 ***State views.*** States, other than Western Australia and the Northern Territory, agreed the the Commission should wait for a new agreement to be finalised.

2.133 Western Australia said that 50% of the payments under NPARIH should be treated as not affecting the State GST shares. It argued that, under the 2016 Update decisison, the Commission has effectively apportioned equal responsibility between the Commonwealth and the States for any past underinvestment in remote Indigenous housing. Western Australia said that the Commission did not provide any supporting evidence for this.

2.134 In addition, Western Australia argued that, prior to the 2010 Review, population growth was not adequately recognised. This reduced the capacity of the fast growing States to invest in remote Indigenous housing.

2.135 The Northern Territory argued that all funding provided under the current National Partnership Agreement on Remote Housing (NPARH) (the interim successor of NPARIH) should be excluded from equalisation because:

- according to the Remote Housing Review, significant additional investment is required, largely due to the inherited underinvestment by previous Commonwealth governments in the Northern Territory's remote housing stock
- the level of additional investment required is not captured in the Commission's assessment of States' housing infrastructure needs, and as such, needs are not assessed.

2.136 Also, the Northern Territory said it would strongly reject any change to the current methodology that reduces the amount of NPARH funding excluded from assessment.

2.137 It is unclear to the Northern Territory how the Commission concluded that all Commonwealth legacy issues would be resolved at the completion of the NPARH. It said that it is clear from the independent review that this is not the case.

2.138 ***Commission decision.*** The Commission notes the views of Western Australia and the Northern Territory. At the time of publication of the report, the Commission's understanding was that funding arrangements for 2018-19 are still being negotiated. Because the Commission does not have sufficient information on the arrangements for 2018-19, the Commission will wait for the agreement to be finalised before considering changes to the assessments.

PUBLISHING QUARANTINED PAYMENTS INFORMATION IN UPDATE/REVIEW REPORTS

2.139 Western Australia has requested the Commission publish, in its annual Update and Review reports, a list of payments that are quarantined by the terms of reference and the amounts of funding each State receives in the relevant assessment years.

2.140 In this update, the Commission has included the amounts of quarantined payments in its supporting documentation on its website. It will continue this practice in the future.

ATTACHMENT A

QUALITY ASSURANCE

A.1 This attachment reports on the quality assurance procedures applied in this update. These procedures aim to ensure the data used in the Commission's assessments are fit for purpose and of the best possible quality, the analysis is accurate and the reporting of the Commission's findings and reasons for decisions leading to them is accurate and transparent.

DATA QUALITY IMPROVEMENT

A.2 Improving data quality is an important aspect of the Commission's quality assurance processes. To this end, data use guidelines and a data protocol were agreed with the States in 2005[1] and have been followed since.

A.3 For this update, the Commission, together with the States, worked to improve the comparability of State provided data used in the assessments.

A.4 The data collection protocol requires the Commission to send a draft copy of requests for new data or information to the States for comment. This is to ensure new requests clearly and accurately specify the data required from the States. For this update, the Commission did not need to send draft data requests to the States.

A.5 The Commission included the previous year's data in all on-going data requests to help data providers identify the information sought and to assist State and Commission staff to identify abnormal movements in the data between the current and the previous year. Commission staff also checked the data on receipt and sought to clarify any unexpected changes with State Treasury officers.

A.6 The Commission also asked the States to clearly identify which datasets used in its assessments could be provided to other State agencies and/or to other third parties to provide as much access to data as possible but also to ensure confidentiality requirements were satisfied.

A.7 Although no formal agreements on data collection were made with other data providers, the Commission has followed the same approach to ensure the data it used were of the best quality.

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1 See *Report on GST Revenue Sharing Relativities – 2010 Review, Volume 2, Attachment A.*

CALCULATION AUDIT PROCESSES

A.8 The Commission completed a rigorous internal audit of all calculations. Internal checks were performed and formally signed off by the assessment officer, the assessment team leader and another officer not involved in the original calculation.

A.9 The Commission also engaged external consultants to check calculations that used new Census data (such as Socio-economic status, Investment and Net lending), and other calculations[2] for Post-secondary education, Housing, Mining revenue, Adjusted budget expenses, National capital, Native title and land rights.

REPORTING OF METHODS, DECISIONS AND RESULTS

A.10 Transparency and accuracy in reporting the assessment methods, decisions and results are important parts of providing high quality outputs.

A.11 The Commission consulted the States on new issues arising in this update that might affect the relativities. Two staff discussion papers on new issues were sent to the States for comment. Commission decisions are set out in *Chapter 2 New issues in this update*. The decisions were made using the assessment and Commonwealth payments guidelines developed in the 2015 Review.

A.12 The Commission undertook a comprehensive program of proof-reading and checking of tables and results to ensure they aligned with the original calculations.

A.13 The Commission continued to post additional material on the Commission's website (https://cgc.gov.au/) to help explain the Commission's work more simply and transparently. This material aims to help the public, as well as the staff of the Commonwealth and State Treasuries, understand the Australian fiscal equalisation system and the Commission's work.

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2 The *2015 Review Quality Assurance Strategic Plan* requires about 25% of all assessments be checked in four updates by external auditors.

COMMISSION TERMINOLOGY

This glossary provides a list of the main terms that have a meaning specific to the Commission. The term 'State(s)' includes the Australian Capital Territory and the Northern Territory.

GLOSSARY

actual per capita (APC) assessment method

The assessed expense or revenue for each State is set equal to its actual expense or revenue. It is used when, in the Commission's judgment, the policies of all States are the same and any differences in expenses or revenue per capita are due to differences in State circumstances.

adjusted budget

A representation of State budgets used by the Commission to calculate the average per capita revenue and expenditures. The scope of the adjusted budget covers all transactions of the State general government sector and urban transport and housing public non-financial corporations, which are in whole or part financed by GST revenue.

administrative scale disability

A disability that measures differences in costs which States incur in providing the minimum level of administration and policy development required to deliver services. It relates to core head office functions and to specialised State wide services provided centrally.

application year

The year in which the average of the assessed GST distributions for each assessment year (expressed as relativities) is to be used to distribute the GST revenue. For example, in the 2018 Update the year of application is 2018-19.

assessed differences (also known as needs)

The financial impact on a State's budget of its disabilities. They are measured, for example, as the difference between assessed expenses and average expenses, assessed revenue and average revenue. Assessed differences can be either positive or negative.

assessed expenses

The expenses a State would incur if it were to follow average expense policies, allowing for the disabilities it faces in providing services, and assuming it provides services at the average level of efficiency. Assessed expenses exclude differences from the average due to policy choices under the control of a State.

assessed GST requirement

A State's requirement for funds from GST revenue in an assessment year. It is measured as its assessed expenses, plus its assessed investment, less its assessed revenue, less assessed Commonwealth payments and less assessed net borrowing.

assessed investment

The expenditure on new infrastructure a State would incur if it were to follow average policies, allowing for disabilities it faces in providing infrastructure, and assuming it requires the average level of infrastructure to deliver the average level of services. Assessed investment excludes differences from the average due to policy choices under the control of that State.

assessed net lending/borrowing

The transaction-based change in net financial worth that a State would require to achieve the average net financial worth at the end of each year. The Commission's method for calculating assessed net lending/borrowing assumes that each State has the average net financial worth at the start of each year.

assessed revenue

The revenue a State would raise if it were to apply the average policies to its revenue base, and raise revenue at the average level of efficiency. Assessed revenue excludes differences from the average due to policy choices under the control of that State, for example a higher or lower tax rate applied by a State compared to the average.

assessment years

The financial years used in a review or an update to calculate the assessed GST requirement, from which an annual relativity is calculated. The Commission uses data for three assessment years (where each assessment year corresponds to a financial year). For example, the GST distribution recommended in the 2018 Update (for the application year 2018-19) is based on the average of three assessment year annual relativities calculated for the most recent completed financial years at the time the relativities are released (2014-15 to 2016-17 assessment years).

average (or Australian average)

The benchmark against which the performance or characteristics of a State are assessed. It is an average derived from the policies or financial data of all States, and hence may be a financial average or a policy average.

average expenses

The average per capita expense, in a category, a group of categories or in total. It is calculated as the sum of expenses of all States, divided by the Australian population.

average revenue

The average per capita revenue, in a category, a group of categories or in total. It is calculated as the sum of State revenues, divided by the Australian population.

backcasting

Changes made to data for assessment years to reflect current or future Commonwealth or State policies. Backcasting is mainly used to reflect major changes in federal financial arrangements. Where required by the Commission's terms of reference, it has also been used to reflect other changes, such as the replacement of one tax with another tax or the abolition of a tax. In effect, backcasting produces notional financial data that simulate a changed distribution of a Commonwealth payment or State revenue collection before they may have actually changed. Actual data for the assessment period are adjusted to reflect what is reliably known to be happening in the application year.

capital assessments

In this report, the term capital refers to the Investment, Depreciation and Net borrowing assessments.

category

A classification of in scope transactions relating to distinct services or revenue sources, used for analytical purposes. In the 2018 Update, the adjusted budget is divided into Commonwealth payments, seven revenue categories, thirteen expenditure categories and net borrowing.

category factor

The combined result of all the disability factors in a category, or where the category is made up of multiple components, the combined disability factors for all of those components. The category factor is expressed as a ratio to the average. For example in an expense category, a category factor of 1.05 means that the State's disabilities require it to spend 5% more than the average to follow the average expense policy at the average level of efficiency.

Commonwealth payments

Payments to States made by the Australian Government, including general revenue grants (other than GST revenue), payments for specific purposes (PSPs) and Commonwealth own purpose expenses. The Commission examines the purpose of each payment using established guidelines to decide whether the payment has an impact on State fiscal capacities.

component

A part of an expense or revenue category that is separated from others in the category because different disability factors apply to it.

cross-border factor

A disability factor that measures the net effects on a State's costs of the use of its services by residents of other States and vice versa.

disability

An influence beyond a State's control that requires it:

- to spend more (or less) per capita than the average to provide the average level of service, or
- to make a greater (or lesser) effort than the average to raise the average amount of revenue per capita.

disability factor

A measure of a State’s use, cost or revenue raising disability, expressed as a ratio of the State's assessed expense or assessed revenue over the corresponding average figure. Policy differences between States are specifically excluded when calculating disability factors. The population weighted average of a disability factor is 1.0.

discounting

Where a case for including a disability in a category is established by the Commission, but the measure of that disability is affected by imperfect data or methods, the Commission may decide to apply a discount. When an assessment is to be discounted, a uniform set of discounts is used (12.5%, 25% or 50%), with higher discounts being applied where there is less confidence in the outcome of the assessment or more concern attached to the data.

distribution

State shares of GST revenue based on the principle of horizontal fiscal equalisation.

distribution model

A formulation, mathematical or otherwise, of the way in which State GST shares (and relativities) are calculated. A mathematical presentation of the model is provided on the Commission’s website (https://cgc.gov.au/).

equal per capita (EPC) assessment method

Each State’s assessed expense or assessed revenue in a category is set equal to the Australian average per capita amount. It is typically used when there are judged to be no material disabilities between the States, or no reliable assessments could be developed due to data or other limitations. Such an assessment means that no needs are assessed for any State and that there is no impact on the GST distribution.

equalisation

See horizontal fiscal equalisation (HFE).

expenditure

This term is used to refer to expenses and capital expenditure.

expenses

Operating outlays under an accrual budgeting framework.

fiscal capacity

The fiscal capacity of a State is a measure of its ability to provide average services, including infrastructure, to its population if it raised revenue from its own revenue bases at average rates and received its actual Commonwealth payments, excluding the GST. Once the GST has been distributed using the Commission's recommendations, State fiscal capacities should be equal.

The relative capacity of each State is a comparison of its fiscal capacity with the average capacity.

Goods and Services Tax (GST) revenue or GST pool

The funds made available by the Australian Government for transfer to the States as untied financial assistance, consistent with the principle of horizontal fiscal equalisation.

grant design inefficiency

A flaw in a method of assessment which would allow a State to influence its relativity by changing its expense or revenue policies (apart from any effect of these policies on the average).

horizontal fiscal equalisation (equalisation)

A distribution of GST revenue to State governments such that, after allowing for material factors affecting revenues and expenditures, each would have the fiscal capacity to provide services and their associated infrastructure at the same standard, if each made the same effort to raise revenue from its own sources, operated at the same level of efficiency and maintained the average per capita net financial worth.

impact on relativities (previously called inclusion), see also no impact on relativities

Treatment applied to a Commonwealth payment that provides budget support for State services for which expenditure needs are assessed. The expenses funded by payments that affect the relativities are assessed in relevant categories and the revenue is assessed on an actual per capita basis.

infrastructure

Infrastructure refers to the stock of physical assets owned by a State's general government sector and its urban public transport and housing public non-financial corporations for the purpose of delivering services. It includes buildings, non-building construction (such as roads) and plant and equipment for economic and social purposes.

investment

Investment refers to capital expenditure less depreciation expenses. It is conceptually equivalent to 'net acquisition of non-financial assets' that appears in the Australian Bureau of Statistics Government Finance Statistics State operating statement.

material, materiality

A test used to assist decisions about whether a separate assessment of disabilities should be undertaken or data adjusted. The materiality levels are defined in terms of the amount of GST redistributed per capita for any State. Different thresholds are used for each. An assessment or adjustment is said to be material if it exceeds the threshold set for it. (See the Assessment Guidelines, Chapter 1 of the 2015 Review Report, Volume 2.)

national capital disability

A disability that measures the additional costs that the ACT incurs because of Canberra's status as the national capital.

national partnership payments (NPPs)

Commonwealth payments to States that support the delivery of specified projects, facilitate reforms, or reward those jurisdictions that deliver on nationally-significant reforms.

National specific purpose payments (SPPs)

Commonwealth payments to States for specific purposes that enable national policy objectives to be achieved in areas that may be administered by States.

native title and land rights disability

A disability that measures differences in costs that States incur because of the operation of the Australian Government's Native Title Act 1993 or the additional and unique costs that the Northern Territory incurs because of the operation of the Australian Government's Aboriginal Land Rights (Northern Territory) Act 1976.

needs

See assessed differences.

net financial worth

Net financial worth is the sum of financial assets minus the sum of liabilities.

net borrowing

The outcome of an operating budget calculated as expenses and expenditure on non-financial assets less State own source revenues and revenues received from the Australian Government.

no impact on relativities (previously called exclusion or out of scope)

Treatment applied to a Commonwealth payment that does not provide budget support for State services or for which expenditure needs are not assessed. Both the payment and the expenses relating to it have no impact on a State's fiscal capacity. Occasionally the terms of reference instruct the Commission to ensure a particular payment has no impact on relativities. (See quarantine.)

payments for specific purposes (PSPs)

Australian government payments to the States for specific purposes in policy areas for which the States have primary responsibility. These payments cover most functional areas of State (and local government) activity, including health, education, skills and workforce development, community services, housing, Indigenous affairs, infrastructure and the environment. PSPs include SPPs, National Health Reform funding, Students First funding and NPPs.

policy average

The average policies as reflected in the practices of the States in the collection of revenue and the provision of services. These averages are usually weighted according to the size of the user or revenue bases in each State.

policy neutral assessment

An assessment in which the policy average is applied to every State. The resultant assessment is, therefore, unaffected by the policies of individual States, other than through the influence of those policies on the averages.

quarantine

The treatment of a Commonwealth payment, and where possible the expense for which it is used, in such a way as to have no impact on the relativities. Quarantining always results from instructions given directly to the Commission in its terms of reference and the term is used only in this context.

ratio of actual expenses to assessed expenses

A ratio that reflects how a State’s policies on the level of services provided and the relative efficiency with which they are provided vary from the average policies. It is measured by dividing actual per capita expense by assessed expense per capita.

ratio of actual investment to assessed investment

A ratio that reflects how a State’s policies on the level of capital provided varies from average policies. It is measured by dividing actual per capita expense by assessed expense per capita.

ratio of actual revenue to assessed revenue

A ratio which indicates the actual effort made by a State to raise revenue relative to the average effort. It is primarily a measure of the deviation of a State's tax rates and effort put into ensuring compliance from average rates and average compliance efficiency. It is measured by dividing actual per capita revenue by assessed revenue per capita.

ratio of assessed expenses to average expenses

A ratio of a State’s assessed per capita cost of providing services at average standards, relative to average per capita cost. It is calculated by dividing per capita assessed expenses by per capita average expenses.

ratio of assessed capital to average capital

A ratio of a State’s assessed capital requirements per capita to the Australian average capital requirement per capita. The assessed capital requirements are what a State would have needed to invest or lend/borrow to have the Australian average level of capital. It is measured by dividing per capita assessed capital by per capita average capital.

ratio of assessed revenue to average revenue

A ratio which indicates the capacity of a State to raise revenue relative to the average. It reflects the size of a State's revenue base per capita relative to the average and is measured by dividing assessed revenue per capita by average revenue per capita.

redistribution

The difference between an equal per capita distribution of GST revenue and one based on the principle of horizontal fiscal equalisation.

regional costs disability

A disability that measures cost differences within a State due to differences in the wages paid and in the price and quantity of other inputs to State services.

relativity

A per capita weight assessed by the Commission for use by the Commonwealth Treasury in calculating the share of the GST revenue a State requires to achieve horizontal fiscal equalisation.

revenue base

A measure of the transactions, activities, or assets that are taxed by the States. Differences between the revenue bases of each State are used by the Commission to determine the relative capacities of each to raise a particular type of revenue.

revenue effort

The intensity of use of a revenue base (the implied tax rate) measured as actual revenue divided by the assessed revenue. It is influenced by the rate of tax or charge, the exemptions, and concessions provided, actual scope of the revenue base in a State, and the effort it put into ensuring compliance.

review

The process in which the Commission reconsiders the methods used to calculate the GST distribution, according to terms of reference given to it. From 1988 onwards, reviews have usually been done every five years. By contrast, an update is conducted every year other than a review year and updates the GST distribution using the methods determined in the last review and the latest financial data.

service delivery scale disability

A disability that measures the additional costs of providing a service where it needs to be delivered but where the delivery is more costly because the population served is small and isolated from other points of service delivery.

Socio-demographic composition disability

A disability that measures differences in both the average use and cost of providing services due to differences between States in the relative size of various socio-demographic groups.

It can reflect differences between States in some or all population characteristics such as age sex structure, socio economic status, Indigenous status and location.

State(s)

Unless the context indicates otherwise, the term 'State(s)' includes the Australian Capital Territory and the Northern Territory.

tax base

See revenue base.

update

The annual assessment of the GST distribution undertaken by the Commission between reviews. Update assessments incorporate new budgetary developments and the most recent available data. In general, the methods used to calculate the GST distribution are those adopted in the most recent review.

user charges

Fees and charges raised by States through the provision of goods or services. In the adjusted budget, user charges for health, post-secondary education, electricity, water and protection of the environment, mining regulation and public transport are deducted from related expenses. Housing user charges are assessed in a separate component in the Housing category. Other user charges are included in the Other revenue category.

wage costs disability

A disability that recognises that otherwise comparable public sector employees in different States are paid different wages, in large part due to differences in labour markets beyond the control of State governments.

ACRONYMS

ABS	Australian Bureau of Statistics
ACARA	Australian Curriculum, Assessment and Reporting Authority
ACTPS	ACT Public Service
APC	Actual per capita
CGC	Commonwealth Grants Commission
CoE	Compensation of Employees
CoES	Characteristics of Employment Survey
CSG	Coal Seam Gas
CSS	Commonwealth Superannuation Scheme
ED	Emergency Department
EPC	Equal per capita
ERP	Estimated Resident Population
GST	Goods and Services Tax
HFE	Horizontal fiscal equalisation
IGA	Intergovernmental Agreement on Federal Financial Relations
IHPA	Independent Hospital Pricing Authority
IRSEO	Indigenous Relative Socio-economic Outcomes (index)
NDIA	National Disability Insurance Agency
NDIS	National Disability Insurance Scheme
NDRRA	Natural Disaster Relief and Recovery Arrangements
NECR	Notional Employer Contribution Rate
NERA	National Education Reform Agreement
NHHA	National Housing and Homelessness Agreement
NISEIFA	Non-Indigenous Socio-economic Index for Areas
NPARH	National Partnership Agreement on Remote Housing
NPARIH	National Partnership Agreement on Remote Indigenous Housing
NPP	National partnership payment
PHE	Public Hospital Establishment
PSP	Payments for specific purposes
PSS	Public Sector Superannuation Scheme
SDC	Socio-demographic composition
SEIFA	Socio-economic indexes for areas
SES	Socio-economic status
SPP	Specific purpose payment
SRS	Schooling Resource Standard
VFI	Vertical Fiscal Imbalance