



1 Treasury Place  
GPO Box 4379  
Melbourne Vic 3001  
Australia  
Telephone: (+61 3) 9651 5111  
Facsimile: (+61 3) 9651 5298  
DX 210759

Mr Greg Smith  
Chairperson  
Commonwealth Grants Commission  
First Floor, Phoenix House  
86-88 Northbourne Avenue  
BRADDON ACT 2612

Dear Mr Smith

**2015 METHODOLOGY REVIEW TELEPRESENCE FOLLOW UP**

Thank you for the opportunity on 29 October 2014 to discuss the progress of the Commonwealth Grants Commission *2015 Methodology Review* and issues of particular importance to Victoria.

I note a number of issues were identified in the telepresence and raised in a follow up email to my staff. For your information, please find attached Victoria's response to these topics including the health assessment, wages, contemporaneity and low socio-economic status disability for other general welfare services.

Please note, the Victorian Government is currently in Caretaker and therefore unable to put forward a government position on any new issues, such as Western Australia's contemporaneity proposal, at this time.

I look forward to the opportunity to respond to significant changes to the proposed methodology put forward in the Draft Report prior to the release of the Final Report.

Yours sincerely

**David Martine**  
Secretary



## **Victorian response to specific issues raised in 29 October 2014 telepresence and follow-up email**

### **HEALTH**

Thank you for a constructive discussion around the issue of substitutability of state and non-state health services in emergency departments. It may be helpful to provide some additional clarifying information surrounding Victoria's position.

We agree with the Commissioners that clinically, there may well be a significant level of substitutability between emergency department services and services provided by a GP. However, for the Commission's purposes it is the patient's behaviour, not an ex-post facto clinical assessment that should be the relevant consideration. Irrespective of clinical opinion on presentation, the relevant ABS data indicates that just 22.6 per cent of patients who attended an emergency department believed they could have been seen by a GP. This should be the upper bound for any estimate of substitutability.

The majority of these patients who attend an emergency department instead of a GP do so because they are unwell outside of normal GP hours. While care provided to these patients may be clinically substitutable with GP services, the level of state service provision required is unlikely to be affected by changes in the level of relative GP throughput in a state or territory. The data strongly suggest that GP throughput data is only relevant to the 2.5 per cent of patients attending an emergency department because the wait for a GP was too long.

We consider that irrespective of any clinical assessment of service substitutability, the level of emergency department use affected by the relative level of GP service provision is likely to be much lower than 40 per cent. A substitutability rate of between 2.5 and 22.6 per cent would be more appropriate.

### **WAGES**

In light of the very large quantum of GST revenue redistributed by this assessment, Victoria considers it is not tenable to postpone addressing known issues with the interstate wages disability until the 2016 Update. In particular, Victoria would like the Commission to reconsider the proposed discount rate and decision not to proceed with a move to a capital city based assessment.

More fundamentally however, the current assessment is not reflective of the actual costs faced by state governments in delivering services, and significantly overstates the scale of any required adjustment. The result has been that the Commission's methods have for many years systematically overstated the cost of delivering services in high wage states, and understated the cost of service delivery in low wage states. This has resulted in a tenfold increase in the level of redistribution associated with this disability since its introduction in 1992–93, despite relative public sector wage levels remaining essentially unchanged.

It is unclear that even the release of an expanded ABS dataset for the 2016 Update will address this issue. Victoria has used its submission in response to the Draft Report to propose a sensible,



middle-ground solution to this problem, that would bring this disability more closely in line with the actual pressures faced by state governments in setting public sector wages. Importantly, Victoria's proposed approach would be policy neutral, reliable, and would remain appropriate whatever the dataset used as the basis for this assessment. We hope that the Commission will give strong consideration to Victoria's proposed approach.

## **CONTEMPORANEITY**

Western Australia has presented the Commission with a proposal which would result in three significant changes to the current methodology:

- assessment to be based on financial estimates for the application year;
- no averaging of assessment year per capita relativities; and
- subsequent corrections for actual financial data.

As the Victorian Government is currently in Caretaker, the following is limited to a factual discussion.

In the *2010 Methodology Review* the Commission stated the contemporaneity principle means that, as far as possible, equalisation should reflect State circumstances in the year the funds are used. However, as the application year is in the future when the GST relativities are determined, to fully meet this principle would require projections of State finances and circumstances which may not be reliable.

The need for reliable data places a constraint on the full realisation of this principle. The need for reliable data results in the Commission determining the GST distribution required to achieve HFE in the years for which actual data are available and assuming that the fundamental structure of those years continues in the application year. An exception is federal financial arrangements where the assessments are adjusted to reflect any major changes that occur between the historical years and the application year.

The use of financial estimates for the application year could require states and territories to produce forward estimates that are at a finer lever of GPC detail than currently used for estimates. Although states and territories have sophisticated forecasting methods, there is still some uncertainty associated with the estimates.

A further complication is that estimates to determine a number of the expense disability factors are based on actual data and would not be available for the application year. Some of the data required are not available for the last assessment year. Basing disability factors on data for years other than the application year would introduce a further degree of uncertainty to the GST relativities.

The proposal from Western Australia argues that it would improve the budgeting of states and territories by spreading revenue volatility of one state across all the states and territories. The current methodology does this, albeit with a lag. However, this lag is known and the state facing own-source revenue volatility would at least have some certainty about its share of GST revenue. Western Australia needs to establish how introducing greater volatility in GST shares would improve budgeting.

The *2010 Methodology Review* recommended that GST distribution is based on the average of the per capita relativities obtained from the three most recent years for which actual data are available. The Commission argued that this averaging smooths the effects of data irregularities and short term events and make the GST shares less volatile.

In the *2015 Methodology Review* Draft Report the Commission restates it considered that basing assessments of the average of the per capita relativities derived from actual data for the last three years provides a balance between reflecting conditions likely in the application year and practicality concerns such as data reliability and stability. Western Australia needs to demonstrate how foregoing data reliability and stability would produce an outcome that is preferable to the current one.

If GST shares were to be based on the financial estimates of the states and territories then there would need to be an adjustment for actual outcomes to ensure that the principles of HFE are met and to prevent any gaming of the GST relativities. This reconciliation of actual to estimated financial estimates would be spread over a number of years.

To illustrate how the reconciliation could occur the following table relates data availability to updates, in the case of the 2012–13 application year, if estimated data had been used for the 2012 Update.

State publication	Time of issue	Update
Budget 2011–12	Mid 2011	2012
Budget 2012–13	Mid 2012	2013
Final budget outcome	Late 2013	2014

This table indicates that the 2012 Update would have needed to use estimates for the second year of the forward estimates period to determine the GST relativities for 2012–13. The revised estimates, which would now be the first year of the forward estimates period would have been available for the 2013 Update. However, it is questionable if the reconciliation should be based on data that are still estimates. It would not have been until the 2014 Update, two years after the application year concerned, that actual data was available for the reconciliation.

It can be seen from the table above that both the current methodology and that proposed by Western Australia involve a two year lag for the use of actual data. It is not clear that the Western Australian proposal represents an improvement.

#### **LOW SOCIO-ECONOMIC STATUS DISABILITY FOR OTHER GENERAL WELFARE SERVICES**

In the *2015 Methodology Review* Draft Report, the Commission’s intention was to assess other general welfare services using the relative proportion of people in the bottom quintile of the ABS’s Socio-Economic Index for Individuals (SEIFI) based on 2011 Census data. However, the ABS will not be updating the SEIFI using the 2011 Census data, nor will it be releasing a family level index (SEIFF). An experimental household level index has been constructed, but this is unlikely to be available in time for the *2015 Methodology Review*.



The task for the Commission is to find an appropriate indicator for the use of other general welfare services. These services include:

- homeless persons' assistance;
- information, advice and referral services;
- prisoners' aid;
- care of refugees;
- premarital education;
- women's shelters;
- general casework services;
- multi-client services (food and clothing) in times of personal and family emergencies and relief of victims of man-made disasters; and
- community and management support.

The potential indicators examined by the Commission were:

- household equalised income;
- homelessness, excluding persons living in 'severely' crowded dwellings; and
- one-parent families with dependents.

The Commission considered that the proportion of one-parent families with dependents in state populations would be a reasonable broad indicator of disadvantage and of the need for spending on other general welfare. The reason advanced was that these families tend to be higher users of welfare services such as temporary accommodation and other support services.

Victoria expressed the view in response to this proposal that, given the coverage of other general welfare services, this indicator appears to be too narrowly based.

The Commission did not consider the Non-Indigenous Socio-economic Indexes for Areas and Indigenous Relative Socio-Economic Outcomes (IRSEO/NISEIFA), proposed in the Indigeneity assessment as a geographic measure of socio-economic status, to be a good indicator for other general welfare services. The reason for this is that while it is an appropriate way to link user characteristics with service use, it is not a good measure of general relative disadvantage. It ignores the likelihood that disadvantaged people live in non-disadvantaged areas. Victoria's response to the Draft Report encouraged the Commission to more carefully consider the use of IRSEO/NISEIFA.

If the Commission does investigate the use of IRSEO/NISEIFA and determines that these are unsuitable then it may be worthwhile giving more careful consideration to deriving an index from equalised total household income. The Commission took the view that this focuses on only one aspect of disadvantage (that is, income) and would be too narrow an indicator of use for other general welfare services.

According to the ABS, equalised total household income can be viewed as an indicator of the economic resources available to a standardised household. It might be expected that households with relatively lower economic resources would be relatively higher users of other general welfare services. This indicator would seem to be worthy of more consideration.



It may be the case that a combined indicator might be required. As Victoria noted in its response to the Draft Report, any indicator chosen is unlikely to provide a complete measure and accordingly at least the minimum discount should be applied.