

WESTERN AUSTRALIA'S FURTHER COMMENTS ON THE REMOTENESS CLASSIFICATION

These comments have been prepared in response to the analysis of issues emailed to States by the Commonwealth Grants Commission (CGC) staff on 27 June 2013.

In that email, it is concluded that:

- for the 2014 Update, the SARIA indexes will be updated for the latest Census data and applied as currently; and
- for the 2015 Review, there is strong preference for changing to ARIA indexes (as used by the ABS).

We support the continued use of SARIA in the 2014 Update, as methodology should not change in updates unless there are materially changed circumstances (which is not the case here).

We do not support what appears to be a rushed decision to change to ARIA indexes in the 2015 Review, but recognise that the CGC needs to progress its research fairly quickly, and some data may be more readily available using ARIA indexes. We support the CGC using ARIA indexes to facilitate its research program, but consider that the assessment methods for regional costs need to be fully considered in the 2015 Review. In this regard, we consider that:

- there are substantial issues around the ability of either ARIA or SARIA indexes to properly reflect needs, or to do so in a policy neutral way
 - even if retained, assessments based on these indexes would need to be supplemented with assessments for regional influences that the indexes do not capture;
- the underlying logic of the SARIA indexes is stronger than for the ARIA indexes in a HFE context, and flaws in the SARIA index can be addressed;
- the evidence that has been put forward to support the change in the capital city classification of Darwin and Hobart needs more work to understand its full significance, and is better interpreted as evidence for reviewing the impact of socio-economic factors and availability of non-state services in the assessments for hospitals and schools;
- the credence given to the use of ARIA indexes in the National Education Reforms is unwarranted; and
- the concern (expressed by all States and Territories) about truncating distance effects could be resolved through empirical analysis.

These issues are addressed below.

CHALLENGES IN USING SARIA/ARIA INDEXES TO REFLECT NEEDS

We understand that the CGC is interested in having a geographical index that provides a guide to regions of Australia that are comparable in terms of:

- unit costs of service (incorporating the quality/cost tradeoffs that States make);
- demands for services (standardised where appropriate for SES, indigeneity and demographic factors; and incorporating the 'remoteness'/quality tradeoffs that States make); and
- use and availability of substitutes for State services (e.g. private hospitals).

Trying to develop an index to capture all three factors is a big ask. Arguably, the ARIA and SARIA indexes have only limited capacity to capture any of these factors.

- The ARIA and SARIA indexes are, roughly speaking, able to capture the population size and distance elements of costs relating to the availability of goods, services, community amenities and social experiences. They capture environmental factors only to the extent that there is a correlation with population size/remoteness. These indexes are particularly poor at capturing local economic conditions that affect living costs such as the accommodation shortages in the Pilbara (to be discussed in our July submission).
- The ARIA and SARIA indexes are not designed to measure service demands. The relationship of service demands to population and distance is an assumption. The impact of environmental conditions and strategic economic importance is not captured (or only indirectly to the extent that there is correlation with population size/remoteness).
- Again, the ARIA and SARIA indexes are not designed to, and in practice do not, measure the private/public split of services. The CGC recognises this in the assessments of schools and public health.

A further concern with these indexes is their lack of policy neutrality. The Western Australian Government is investing substantial funds into the development and population growth of key towns in the Pilbara (e.g. Pilbara Cities Initiative and housing programs). This investment is essentially unrecognised in the CGC's current assessments. A successful outcome from this investment will lead to cities that grow faster and areas that become less 'remote' under the ARIA/SARIA indexes (e.g. a city that passes the 48,000 population threshold will lead to it and the surrounding region becoming less 'remote'), leading to a possible reduction in grant funding.

- In effect, the Government's investment can potentially attract an explicit GST penalty (as well as the broader implicit GST penalty from the improved revenue raising capacity that could result).

Underlying logic of the SARIA/ARIA indexes

In our view, the SARIA indexes have a better underlying logic in respect to the separate treatment of capital cities, and not truncating the effects of distance.

The ABS paper *ASGC Remoteness Classification: Purpose and Use (Census Paper No. 03/01)* notes (see pages 10-11) that ARIA's truncation of distance is a weakness, but considers that in practice it will not affect the remoteness of communities. However, the CGC has calculated that Broome, Karratha and Port Hedland would all be reclassified from Very Remote to Remote if SARIA scores were truncated.

The CGC has attempted to justify the reclassifications on the basis that these towns are larger than other Very Remote towns, and so less affected by remoteness. However, this is not a logical argument, as it is fundamental to the methodology that different combinations of distance and population size can yield the same remoteness classification. For example, using the CGC argument, a similar concern could be raised if these towns are classified as Remote – they are at a further distance, and so more affected by remoteness, than other similar size Remote towns.

This ABS paper does support the CGC's view that smaller capital cities should not be recognised as equivalent to larger capital cities as it would make Tasmania and NT less remote. However, from a cost perspective, the relative remoteness of Tasmania and NT are recognised in HFE through the assessment of interstate costs (mainly wages).

We consider that it is more appropriate to rate capital cities equally for intrastate dispersion purposes, as they are providers of last resort and providers of specialty services. Reflecting that they are the seat of governments, they also tend to have the most balanced urban economies, greatest amenities, greatest social networking opportunities for professionals, and most cosmopolitan environment.

The 'impermeable border' assumption used by SARIA is acknowledged to be a weakness, which however can be readily addressed through a 'semi-permeability' assumption (recognising that some impermeability is justified for State services).

EVIDENCE THAT DARWIN AND HOBART ARE EXCEPTIONAL

We continue to have difficulty with using the two charts put forward by the CGC, on Medicare bulk billing rates and school completion rates, to justify a different treatment for Darwin and Hobart.

- Variations occur across the capital cities (e.g. Canberra is acknowledged to have a low Medicare bulk billing rate and high school completion rate), and may well occur more widely across the States, but only Darwin and Hobart are singled out.

- The SEIFA standardised school completion rates could be influenced by a number of factors, including mobility, differences between the SES of students and the SES of the general population, unemployment rates and cultural factors.
- Overall, these charts highlight research issues for the health and education assessments, potentially requiring disability allowances such as those already assessed for non-state services in the schools and public health categories, and are not suitable evidence for the remoteness indexes.

NATIONAL EDUCATION REFORMS (NER)

The CGC notes that the ARIA indexes have been used to help derive the NER loadings for educational disadvantage. However, the NER methodology is non-transparent and has been criticised as being flawed by the Melbourne Institute. A potential indicator of problems with the NER methodology is the need for Western Australia to be given a special 11% 'State relativity' adjustment.

TRUNCATION EMPIRICAL ANALYSIS

As noted above, all States and Territories have expressed reservations about truncating the impact of distance, a view shared in principle by the ABS. Given time, this issue can be further explored empirically, both in terms of the actual impact of distance on costs, and the difference it could make to the 'remoteness' rating of communities.

Western Australian Treasury

July 2013