

**Submission
No 1**

INQUIRY INTO COMMONWEALTH SUPPORT FOR VICTORIA

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Victoria's share of revenue from the GST

Submission to the Victorian Legislative Assembly Economy and Infrastructure Committee's Inquiry into Commonwealth support for Victoria

by

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Introduction

On 4th August 2021, Victoria's Legislative Assembly referred to its Standing Committee on the Economy and Infrastructure for consideration and report "various issues associated with the inadequacy of Commonwealth support for Victoria", including "Victoria's share of federal GST funding" and "the expiration of the 'no worse off' GST guarantee".

This is a reference to a provision in the 'agreement' between the Commonwealth and State and Territory Governments reached in 2018 that, at least through the 2026-27 financial year, no state or territory would receive less under the GST revenue-sharing arrangements then agreed than it would have done under the arrangements which that agreement superseded – and that the Commonwealth Government would make additional payments to states and territories to the extent needed to meet that 'guarantee'.

The author of this submission is a resident of Tasmania, but lived in Victoria for almost 32 years (between 1983 and 2014) and continues to regard Victoria with affection.

'Horizontal fiscal equalization'

Australia has a federal system of government, in which state (and, since 1978, territory) governments typically play an important role in shaping and implementing public policies with regard to education, health, housing, transport, the maintenance of law and order, and other functions, which in turn have a key influence on the well-being of and life opportunities available to their citizens.

Reflecting the relative importance of the functions for which they are responsible, state and territory governments have over the past twenty years accounted for 40% of total 'operating' spending by all levels of government in Australia, and for almost 50% of all 'investment' spending by governments (or 58% of all 'investment' spending if public enterprises are included) (ABS 2021).

However, because of the way in which revenue-raising powers were allocated as between the Commonwealth and the States in the Australian Constitution (and the way in which those provisions in the Constitution have been interpreted by the High Court of Australia over many years), the states and territories have on average raised only 16% of the taxation revenue collected by all levels of government over the past twenty years. Even allowing for other sources of revenue available to state and territory governments (such as mineral royalties, fees and charges for government services), the states and territories typically finance only about half of their total expenditures from their own resources, and are reliant on grants and subsidies from the Commonwealth for the remainder.

As Australia's second Prime Minister, Alfred Deakin, foresaw, the Constitution left the states "legally free, but financially bound to the chariot wheels of the Commonwealth" (Deakin 1902).

As a result, Australia's federal system has historically been characterized by a much higher degree of 'vertical fiscal imbalance' than other federations (such as the United States, Canada, Germany and Switzerland) – that is, Australian state and territory governments have been more reliant on 'fiscal transfers' from the national government than their counterparts in other federations (OECD 2014: 99). This 'vertical fiscal imbalance' was greatly increased by the Commonwealth's assumption of a monopoly of income taxing powers in 1942 – ostensibly as a 'temporary war time measure', but one which has remained in place ever since, despite occasional attempts to 'hand back' income-taxing powers to the states (Mathews and Jay 1972: 171-77 and 191-3).

The fact that Australia's state and territory governments are so unusually dependent on transfers from the national government gives Australia's national government the potential to exercise considerably greater influence over the *spatial* distribution of revenue (and hence spending) than occurs in other federations where sub-national governments are more reliant on their own ability to raise revenues.

And this is an influence which Australian Commonwealth governments have chosen to exercise, from the earliest days of the Australian federation.

As early as 1910, the Commonwealth commenced making 'special grants' to Western Australia and Tasmania, which were the 'financially weakest' states during the years immediately after federation (Mathews and Jay 1972: 93). Formal inquiries into the effects of federation on those two states in the 1920s, and another into the effects of federation on South Australia, resulted in annual payments being made by the Commonwealth to all three states by the early 1930s.

Following the overwhelming vote by Western Australians to secede from the federation at a referendum held in April 1933 – the presumed 'right' of which was ultimately denied by a Joint Select Committee of the UK Parliament (Musgrave 2003: 110-23) – the Commonwealth Grants Commission was established for the specific purpose of making recommendations for special assistance grants to offset the financial difficulties of the smaller states. In its third report, published in 1936, the Commission spelled out the principle which has guided its deliberations ever since:

"Special grants are justified when a State through financial stress from any cause is unable efficiently to discharge its functions as a member of the federation and should be determined by the amount of help found necessary to make it possible for that State by reasonable effort to function at a standard not appreciably below that of other States" (Commonwealth Grants Commission 1995: 42).

This principle has become known as 'horizontal fiscal equalization' (or HFE). It was embedded in the legislation under which the Commonwealth agreed to share revenue from income tax with the states as part of the Fraser Government's "new federalism" policy:

"the respective payments to which the States are entitled under this Act should enable each State to provide, without imposing taxes and charges at levels appreciably different from the levels of the taxes and charges imposed by the other States, government services at standards not appreciably different from the standards of the government services provided by the other States ... taking account of differences in the capacities of the States to raise revenues ... and differences in the amounts required to be expended by the States in providing comparable government services" (CGC 1995: 139-40).

The 'horizontal fiscal equalization' objective was maintained when 'tax sharing grants' were replaced by 'financial assistance grants' in the mid-1980s, and when the Northern Territory and subsequently the Australian Capital Territory became self-governing in 1988 and 1993, respectively.

And it was specifically imported into the arrangements for distributing revenue from the GST, which commenced in 2000, among the states and territories. Section 8 of the 1999 *Inter-governmental Agreement on the Reform of Commonwealth-State Financial Relations* explicitly provided that "the Commonwealth will distribute GST revenue grants among the States and Territories in accordance with horizontal fiscal equalisation (HFE) principles" (Howard 1999).

Australia goes further in the pursuit of 'horizontal fiscal equalization' than any other country with a federal system of government (Garnaut and FitzGerald 2002: 4; Pincus 2008: 8). That's in large part because it can, given the unusually high degree of 'vertical fiscal imbalance' in the Australian federation, noted earlier.

And the fact that it has is an important reason why the 'gaps' between Australia's richest and poorest states – as measured, for example, by differences in per capita household disposable income – are significantly less than those between the richest and poorest states or provinces in other federations (Eslake 2017). This is something which, surely, should be seen as a 'Good Thing', not something to be regretted.

There is, inevitably, some trade-off between the objectives of 'equity' and 'efficiency' (in the economic sense of that term) (see, eg, Okun 1975) – although recent research by OECD and IMF economists (among others) suggests that trade-off is not as simple or unambiguous as previously believed (see, for example, Wilkinson and Pickett 2009; Causa et al 2014; Cingano 2014; Ostry et al 2014; Dabla-Norris et al 2015).

The proposition that the pursuit of 'horizontal fiscal equalization' in Australia has had the effect of discouraging state and territory governments from pursuing growth-enhancing economic reforms (including tax reform) for fear that it would adversely affect their shares of revenue from the GST has been advanced by many who have advocated for a less ambitious system of HFE, sometimes to the point of replacing it with an 'equal-per-capita' distribution (see for example (Garnaut and FitzGerald 2002a: 133-153; Ergas and Pincus 2011; and Business Council of Australia 2017: 6-7).

That view was rejected as long ago as 1993 by the Industry Commission (the precursor to the Productivity Commission), which pointed to "a lack of conclusive empirical evidence about the efficiency costs of fiscal equalization", leading it to conclude that "a case for radical reform of fiscal equalisation has not been established" (Industry Commission 1993: xxx).

Similarly, the 2012 GST Distribution Review commissioned by then Federal Treasurer Wayne Swan – whose three members included two former state premiers (of Victoria and New South Wales) who, when in office, had been vigorous proponents of more limited horizontal fiscal equalization – concluded that "the current system can and does create perverse incentives in theory, but that there is little evidence of those incentives having any effect in the real world. In particular, there is no evidence that HFE acts as a material disincentive to State tax reform" (Brumby, Carter and Greiner 2012: 135).

Nonetheless, this view re-surfaced in the Productivity Commission's inquiry into HFE, which was the basis for the changes to the basis for determining the distribution of GST revenues 'agreed to' in 2018.

The Productivity Commission acknowledged that it could not find any convincing evidence that states or territories had eschewed productivity- or growth-enhancing reforms for fear of adversely affecting their GST revenue shares. But it then went on to assert that "an absence of evidence is not equivalent to evidence of absence" (Productivity Commission 2018: 112).

This is the same 'logic' that was used by the US Administration and the British and Australian Governments to justify their invasion of Iraq in 2004 – despite the absence of any evidence that Saddam Hussein possessed 'weapons of mass destruction' or had been in any way involved in the terrorist attacks on the United States on 11th September 2001.

And in that case, as we now know, 'absence of evidence' was indeed 'evidence of absence'.

The 2018 changes to the basis for sharing GST revenues

The Productivity Commission's Inquiry was commissioned by then Treasurer Scott Morrison in 2017, in response to long-standing complaints by successive Western Australian Governments (of both major political persuasions) about the decline in its share of GST revenue as a result of the enormous improvement in its 'fiscal capacity', relative to that of the other states and territories, flowing from the 'mining boom' – which saw WA's mineral royalty revenue increase from less than \$700 million in 2000-01 to over \$6 billion in 2013-14, then decline to \$4.1 billion in 2015-16, before beginning to increase once again as increased iron ore production and export capacity came 'on stream' and the iron price began to rise again¹.

Because a state's capacity to raise revenue from its own sources is one of the principal things which the Grants Commission takes into account (along with the demand for state public services and the unit cost of providing them) in determining how the revenue from the GST should be carved up, WA's share of GST revenue fell from a peak of \$4.0 billion in 2007-08 to \$1.9 billion in 2015-16 (although it should be noted that this drop was much smaller than the increase in WA's mineral royalty revenues over this period).

Western Australia was particularly aggrieved that its 'relativity' – its share of the revenue from the GST relative to its share of Australia's total population – had fallen to less than 30% by 2015-16, much lower than any other state's or territory's had ever been since at least 1980-81.

The Terms of Reference given to the Productivity Commission were 'loaded' in such a way as to encourage it to produce a result that would find favour in Western Australia (Morrison 2017)².

¹ Perhaps not co-incidentally, the commissioning of this Inquiry also followed the Liberal Party's loss of office in Western Australia at the state election held on 11th March that year.

² Echoing the advice sometimes attributed to the Leader of the Liberal Party in the Senate at the time of 'the Dismissal' in 1975, and during most of Malcolm Fraser's Prime Ministership, Reg Withers – who was also a Western Australian – and also given by Sir Humphrey Appleby in an episode of the BBC sitcom [Yes Minister](#) – "never to set up an inquiry unless you know in advance what its findings will be".

The first paragraph of those Terms of Reference enjoined the Commission to “consider the influence the current system has on productivity, efficiency and economic growth, including the movement of capital and labour across state borders; the incentives for the States to undertake fiscal (expense and revenue) reforms that improve the operation of their own jurisdictions, and on the States’ abilities to prepare and deliver annual budgets”, words which echoed the complaints long made by Western Australian state governments.

More specific instructions asked the Commission to consider “policies affecting energy and resources, noting the uneven distribution of natural resources across the nation”, and whether “the present HFE formula, may have the effect of producing a disincentive for a State to develop a potential industry or raise a royalty rate for an existing industry at an appropriate time” – again, reflecting the arguments previously advanced by Western Australian state governments.

The legislation enacting the response of the Morrison Government (as by then it was) to the PC Report had the Orwellian-sounding title of the [Treasury Laws Amendment \(Making Sure Every State and Territory Gets Their Fair Share of GST\) Bill 2018](#) (a form of legislative nomenclature which has become commonplace in the United States, but is comparatively rare in Australia).

This legislation made two important changes to the (long-standing) principles which the Grants Commission uses in making its recommendations as to how the revenue from the GST should be distributed among the states and territories:

- instead of being required to recommend a distribution of GST revenues which would allow each state and territory government to provide public services at the same standards as those of the ‘fiscally strongest’ state, the Grants Commission’s objective would change over a five year period beginning in 2021-22 to that of allowing each state and territory government to provide public services at the same standard as the ‘fiscally stronger’ of New South Wales and Victoria; and
- irrespective of the outcome of those recommendations, from 2022-23 onwards no state or territory would receive less than a so-called ‘floor’ of 70% (and from 2024-25 75%) of what it would receive under a notional ‘equal per capita’ distribution of the revenue from the GST.

These changes were clearly intended to result in Western Australia getting a larger share of the revenue from the GST than it would have done had they not been made:

- when Western Australia is the ‘fiscally strongest’ state – as it has been for most of the past fifteen years – the first of these changes means that it is no longer the ‘benchmark’ to which the other states’ and territories’ fiscal capacity is raised, which in turn means, in effect, that its share of GST is less adversely affected by the greater capacity which it has to raise revenue from (in particular) mineral royalties, when the prices of its mineral resources are especially elevated; and

- if the Grants Commission's assessment of the distribution of GST revenues required to ensure that all states and territories' fiscal capacities were at least equal to that of the stronger of NSW or Victoria were to result in a state getting less (in 2022-23 and 2023-24) 70%, or (from 2024-25 onwards) 75% of what it would have received under a notional equal-per-capita distribution – a position which only Western Australia is likely to be in – then that assessment is over-ridden by the new 'floor' provisions.

These changes were clearly intended to result in Western Australia getting a larger share of the revenue from the GST than it would have done, had they not been made.

And because the distribution of any fixed sum – such as the revenue from the GST in any given year – is inherently a 'zero sum' game, any change which results in WA being better off *necessarily* makes the other states and territories (as a group) worse off.

In order to forestall the obvious objections from the other states and territories, the legislation implementing these changes also provided for a 'transitional guarantee' whereby the Federal Government would, from 2022-23 through 2026-27, 'top up' the GST revenue 'pool' so that no state or territory would receive less than they would have done had the previous arrangements continued³.

At the time when these changes were 'agreed', it was explicitly assumed that the iron ore price – which was then around US\$65/t (having fallen from a peak of US\$155/t in February 2011 to a low of less than US\$45/t in early 2016 before recovering) – would remain at around US\$55/t.

On the basis of that assumption, the Federal Government envisaged that the 'transitional guarantee' that no state or territory would be worse off could be met by 'topping up' the GST 'pool' by \$600 million per annum from 2021-22 onwards (indexed in subsequent years to the growth rate of total GST collections), plus an additional \$250 million per annum (similarly indexed) from 2024-25 onwards.

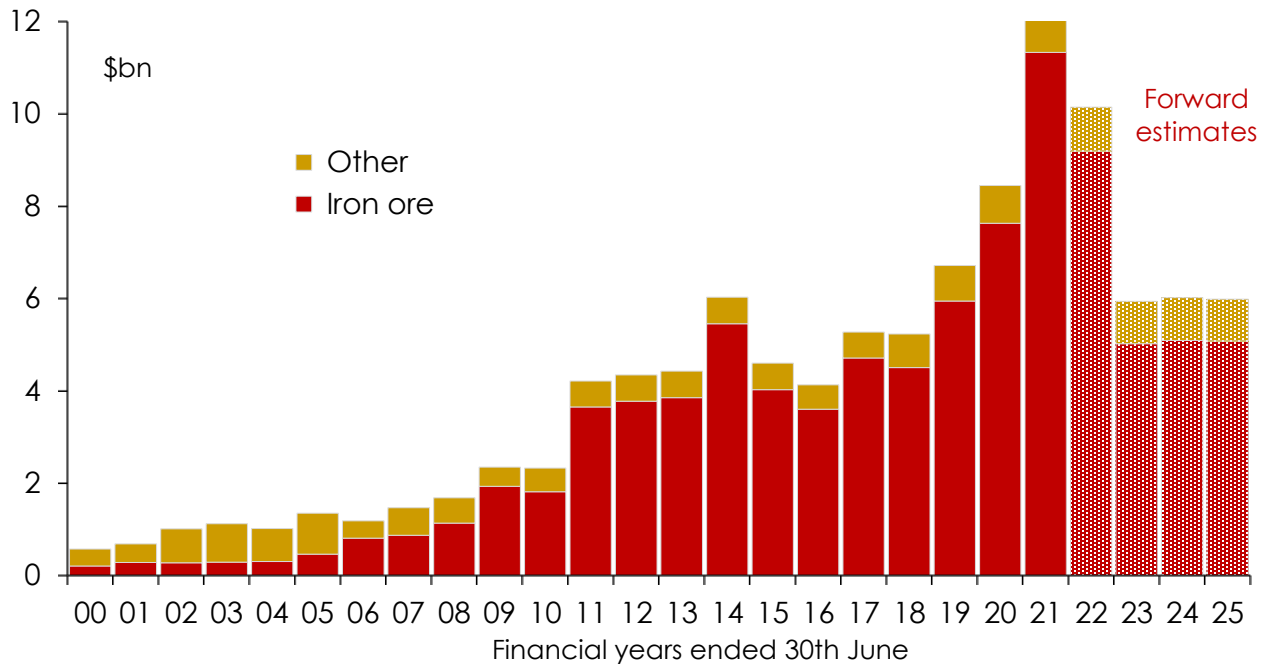
However, the assumption about the iron ore price turned out to be wrong.

The iron ore price continued to recover, peaking at over US\$210/t in June and July this year (although it has since fallen sharply, to just over US\$100/t at the time of writing).

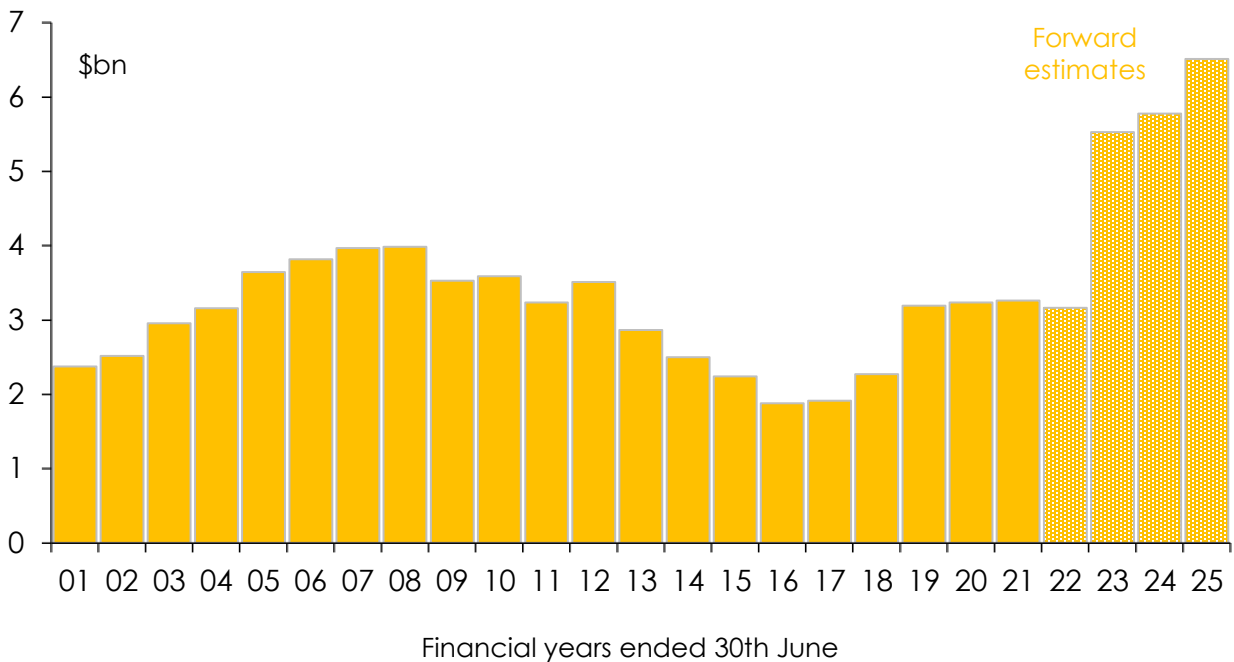
This has been a bonanza for Western Australia – its iron ore royalty revenues in the 2020-21 financial year topped \$11 billion, more than two-and-a-half times the \$4.3 billion which had been forecast for 2020-21 in its 2018-19 Budget (Government of Western Australia 2018: 85 and 2021: 78) (Chart 1).

By contrast, Western Australia this year expects to receive \$5.4 billion from the GST (including \$2.1 billion as a result of the 70% 'floor' under its relativity) – which is \$300 million more than it had forecast in its 2018-19 Budget (Chart 2).

³ These 'top-up payments' were in addition to those which the Government began making to Western Australia in 2018-19, and which continue through to the current financial year, so as to meet its 'demand' for no less than 70% of an equal per capita distribution.

Chart 1: Western Australia's mineral royalty revenues

Source: Government of Western Australia (2021) and previous years' equivalents.

Chart 2: Western Australia's share of GST revenues and 'top up' payments

Source: Government of Western Australia (2021) and previous years' equivalents.

In other words, the 2018 changes represent for Western Australia what Chinese President Xi Jinping would call a “win-win outcome” – whatever happens to the iron ore price, Western Australia “wins”:

- if the iron ore price goes down, Western Australia's share of the revenue from the GST goes up, as it would have done under the pre-2018 arrangements:
- but if the iron ore price stays up, Western Australia in effect gets to ‘keep’ a larger share of the resulting increase in mineral royalty revenues (since its share of revenue from the GST no longer falls by as much as it would have done under the pre-2018 arrangements)⁴.

Because the iron ore price has exceeded (by a wide margin) the assumptions which were made in 2018, the cost to the Federal Government of the ‘transitional guarantee’ that no state or territory would be worse off as a result of these changes has risen substantially.

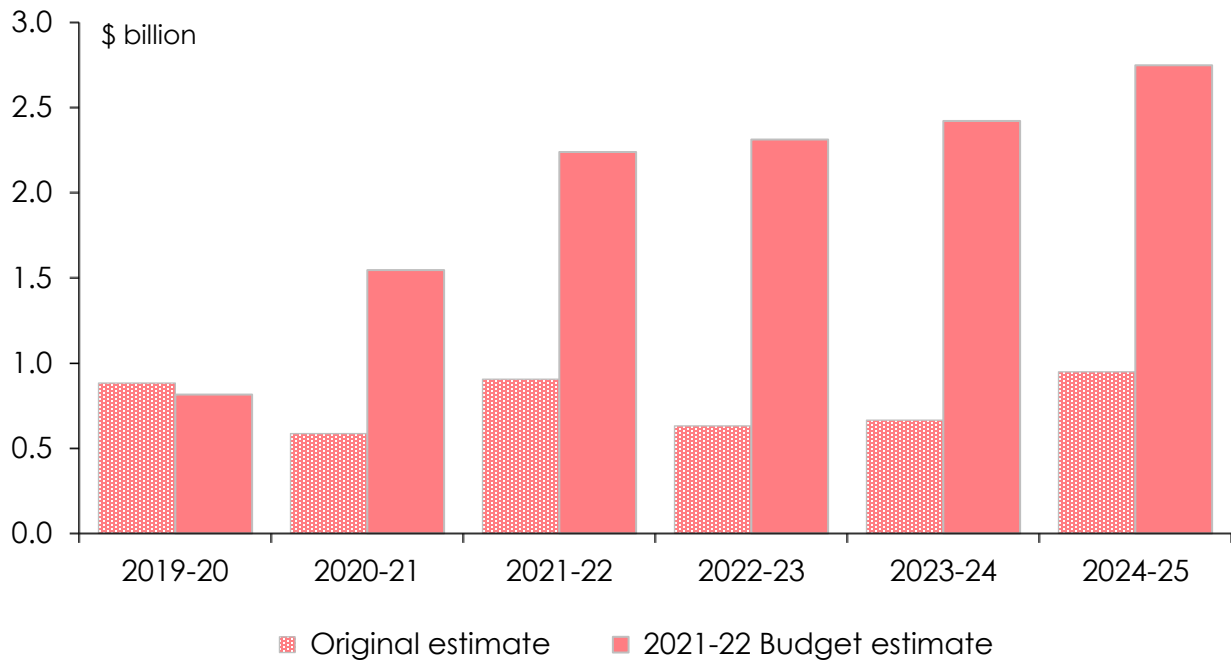
The Federal Government's initial response to the Productivity Commission inquiry estimated the cost of the ‘boost’ to the GST pool required to fund the ‘transitional guarantee’ between 2019-20 and 2026-27 would amount to \$5,201 million (Australian Government 2018: 21) – of which, \$3,733 million would be spent between 2020-21 and 2024-25 inclusive. As shown in Chart 3, the 2021-22 Federal Budget Papers indicate that the cost of the ‘transitional guarantee’ to the Federal Government between 2020-21 and 2024-25 has risen to \$11,269 million – an increase of over \$7.5 billion or 202% (Frydenberg and Birmingham 2021: 100)⁵.

This \$11.3 billion is money which the Federal Government will be adding to the already large budget deficits incurred or projected over this period, in order to transfer an equivalent amount to the only government in Australia (and one of just a handful in the entire world) which is expecting to run budget surpluses – something which to this author seems outrageous (Eslake 2021).

As the New South Wales Government observed in its 2021-22 Budget Papers, “these dollars could have been better spent on productivity-enhancing reforms that support the post-pandemic recovery” (Perottet 2021: 4-14).

⁴ Note that if the iron ore deposits which provide the basis for so much of Western Australia's above-average ‘fiscal capacity’ had been located at, say, Broken Hill, rather than in the Pilbara, under the post-2018 arrangements New South Wales' share of GST revenues would fall by more than Western Australia's, because New South Wales is (in effect) the ‘benchmark’ to which other states' fiscal capacities are to be raised, whereas (as part of the 2018 changes) Western Australia no longer is, even though its ‘fiscal capacity’ is stronger than that of New South Wales.

⁵ The Federal Budget Papers don't disclose what assumptions have been made – in particular as regards the iron ore price – in deriving the forward estimates of the cost of meeting the ‘transitional guarantee’ (although it is known that they are different from the assumption made in the ‘Economic Outlook’ section of *Budget Paper No. 1* that the iron ore price falls to US\$55/t by March next year).

Chart 3: The cost (to the Commonwealth) of the 'transitional guarantee'

Sources: Australian Government (2018: 21); Frydenberg and Birmingham (2021: 100).

As things currently stand, from 2027-28 onwards the cost of any shortfall between the amounts which the Federal Government committed in 2018 (which at the time were forecast to be \$1.1 billion in 2027-28 and \$1.2 billion in 2028-29) and the increase in Western Australia's share of GST revenues (relative to what it would have received had the 2018 changes not been made) will be borne by the other states and territories.

This is a prospect which should be of considerable concern to Victoria.

Why all this matters for Victoria

Victorian Governments have traditionally been advocates of changes to the long-standing 'horizontal fiscal equalization' principles which have served as the basis for the Grants Commission's recommendations for distributing Commonwealth 'general purpose' funding (from 1980-81 through 1999-2000) and (since 2000-01) revenue from the GST among the states and territories.

Indeed, in 2002 Victoria joined with New South Wales and Western Australia in commissioning a 'Review of Commonwealth-State Funding' which recommended that the revenue from the GST be allocated on an equal per capita basis, apart from "a flat amount calculated to cover the irreducible minimum overhead costs of government", and that the Grants Commission revert to its pre-1980 role of recommending 'special grants' for states "experiencing severe financial difficulty" (Garnaut and FitzGerald 2002b: 3-4).

This stance stems from Victoria's historical position as one of Australia's fiscally stronger states – something which is also reflected in Victoria's designation, in the 2018 changes to the GST distribution arrangements, as one of the two states which could serve as an 'equalization benchmark' for sharing the revenue from the GST from 2021-22 onwards.

It has also been reflected in Victoria's depiction of itself as a 'donor state' (see eg Victorian Government 2012: 28). That's because Victoria's 'relativity' (its share of revenue from the GST, or prior to the introduction of the GST its share of general purpose payments from the Commonwealth, relative to its share of Australia's total population) has always been less than 1 – that is, Victoria has always received less than it would have done under a notional equal-per-capita distribution.

Victoria was the 'fiscally strongest' state between 1997-98 and 2002-03, according to the Grants Commission's annual assessments. However neither Victoria nor New South Wales, when it was the 'fiscally strongest' state (between 2003-04 and 2004-07) have every been as 'fiscally strong' as Western Australia has been for most of the period since 2007-08 (Commonwealth Grants Commission 2016: 9).

The only reason that Western Australia's 'relativity' has fallen to 'unprecedented' lows during this period (one of Western Australia's principal grievances with the pre-2018 system) is because Western Australia's 'fiscal capacity' has exceeded that of the other states and territories by a margin which is also without any precedent.

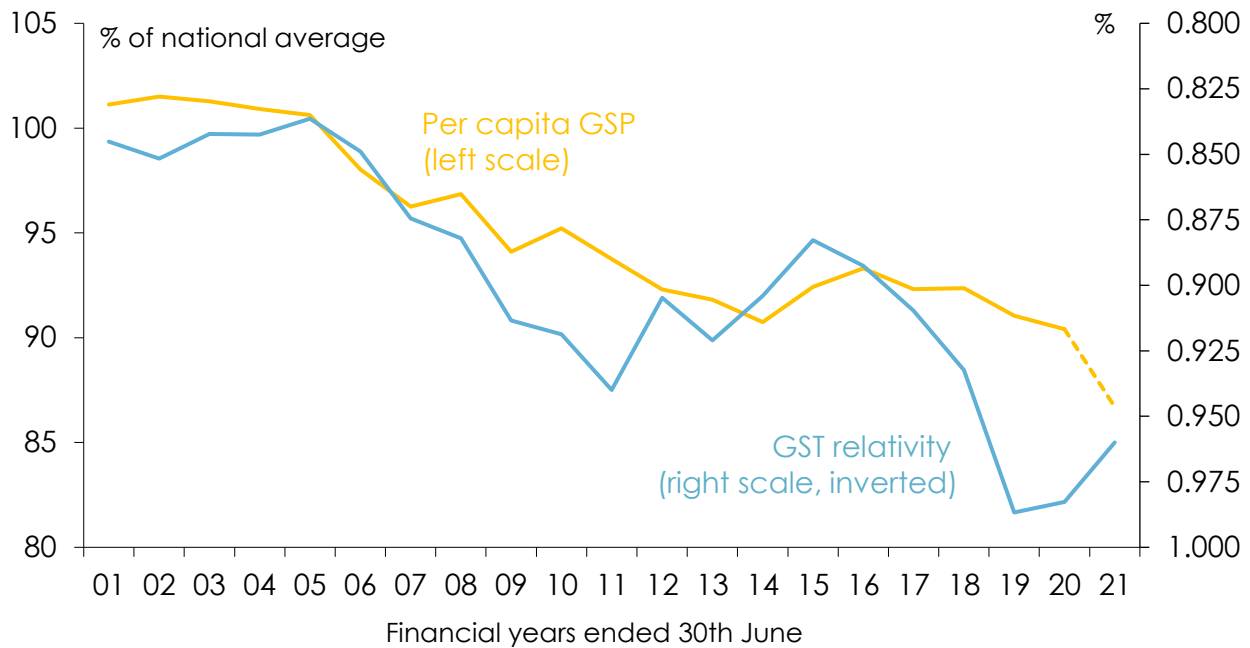
Victoria's above-average 'fiscal capacity', as assessed each year by the Commonwealth Grants Commission, is entirely the result of its 'below-average expense requirement'.

That is, according to the Grants Commission, Victoria doesn't need to spend as much per head of population as other states and territories in order to provide public services of the same 'standard' as the average of all states and territories. That's largely because a smaller proportion of Victorian students attend government schools than in other states and territories (on average); because Victoria has a relatively smaller Indigenous population than other states and territories, and a smaller proportion of its population living in remote areas; and because as a relatively 'compact' state (by comparison with, for example, Queensland or Western Australia) it is more able to achieve 'economies of scale' in public administration (Commonwealth Grants Commission 2020: 37). The one significant exception to this is that the Grants Commission has in recent years assessed that Victoria has an 'above average' urban transport investment requirement, reflecting above-average population growth in Melbourne (at least prior to 2020).

Victoria's 'advantages' on the expenditure side of its budget are partially offset by what the Grants Commissions assesses as its 'below-average revenue raising capacity' – largely due to below-average mining production, but also to a slightly below-average capacity to raise revenue from payroll tax (because Victorian average earnings are slightly below the national average).

Victoria's 'disadvantages' in raising revenue appear to have become more significant over time. As a first approximation, a state or territory's 'revenue raising capacity' can be illustrated by its per capita gross state product (GSP), relative to the average of all states and territories. Victoria's per capita GSP has fallen from around 1% above the average of all states and territories at the turn of the century, to almost 10% below the national average in 2019-20 (Chart 4).

Chart 4: Victoria's per capita GSP relative to the national average and its GST relativity



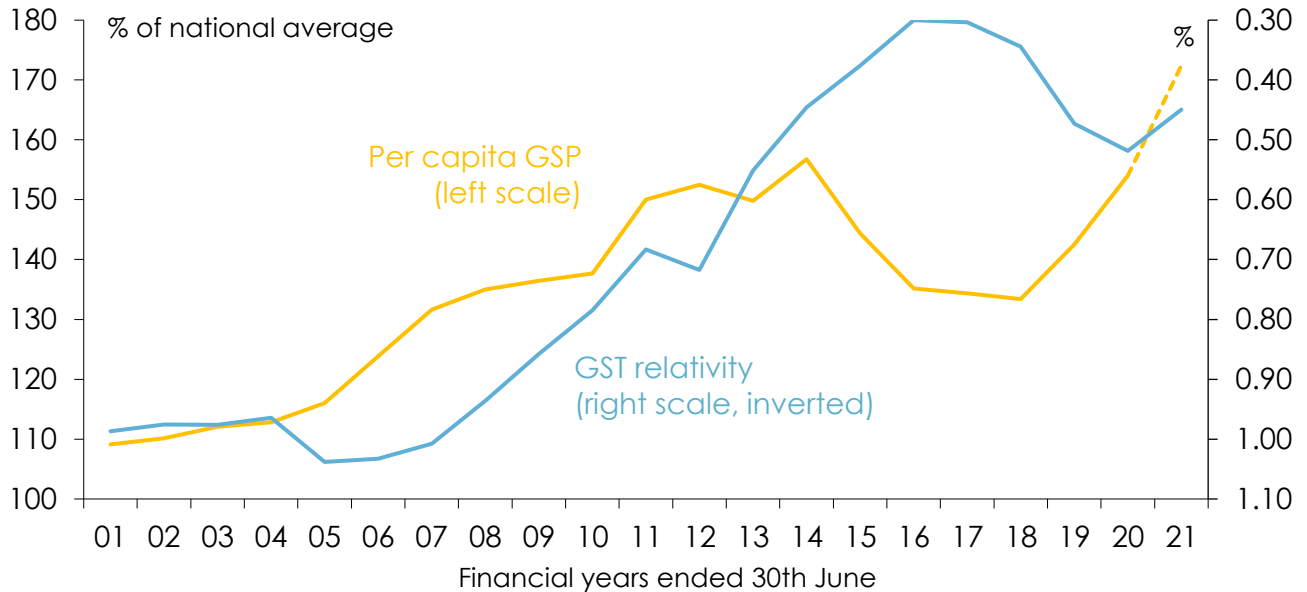
Note: 2020-21 GSP figure based on State Budget estimates. Sources: ABS (2020); Commonwealth Grants Commission (2021).

By contrast, Western Australia's per capita GSP has risen from about 10% above the national average in the early years of this century to more than 50% above the national average in 2019-20 – a margin which, as noted earlier, is without precedent in at least the last sixty years – and is likely to have been more than 70% above the national average in 2021-22, based on WA Treasury estimates in the most recent State Budget (Chart 5).

However, variations in Western Australia's 'fiscal capacity' (above a certain level) are now precluded from being fully reflected in its GST relativity as a result of the changes introduced in 2018.

As previously noted, states and territories other than Western Australia are insulated from the reductions in their shares of revenue from the GST flowing from the 2018 changes until the 2027-28 financial year by the Federal Government's 'transitional guarantee'. However, unless this guarantee is extended, from that year onwards, the cost of the increases in the share of GST revenues going to Western Australia will be borne by the eastern states and territories.

Chart 5: Western Australia's per capita GSP relative to the national average and its GST relativity



Note: 2020-21 GSP figure based on State Budget estimates. Sources: ABS (2020); Government of Western Australia (2021); Commonwealth Grants Commission (2021).

The Victorian Treasury has modelled the possible impact on each state and territory's GST revenue in 2027-28 (after the 'no-worse-off' transitional guarantee expires) under each of six different scenarios, compared with what might have been expected under the pre-2018 arrangements (Table 1 on page 14). Under every one of these scenarios, Victoria's share of GST revenue declines, by between \$67 million and almost \$1,200 million. New South Wales and Queensland are also 'losers' under every scenario, while the smaller states and territories also 'lose' under most scenarios other than a significant fall in WA's mining royalty revenues.

This year's Victorian Budget Papers conclude that allowing the no-worse-off guarantee to expire (as provided for in the Commonwealth legislation imposing the 2018 changes) "impedes not only states' ability to invest in vital services for their citizens now, such as education, health and mental health – but also their ability to plan effectively into the future" (Pallas 2021: 185).

Tasmania's Treasury has undertaken similar modelling, which suggests that Tasmania will lose \$83 million in 2027-28 (more than projected by Victoria's Treasury under any of its six scenarios) (Gutwein 2021: 74). This year's Tasmanian Budget Papers, like Victoria's, conclude that this loss in GST revenue "could significantly impact Tasmania's ability to provide essential services, such as health, education and emergency services".

Although Tasmania's Treasury didn't provide explicit estimates of the expected losses of GST revenue for other states and territories, visual inspection of a chart depicting that modelling suggests that, in its opinion, Victoria's loss could be of the order of about \$180 per head, or around \$1.3 billion (which is more than implied by Victoria's own modelling).

Table 1 – Difference in GST distribution based on former and new system, 2027-28 (\$m)

Scenario	NSW	Vic	Qld	WA	SA	Tas	ACT	NT
1: NSW and Vic stamp duty growth slows	-250	-196	-124	1,636	-17	2	-7	29
2: A decrease in WA's mining revenue	-105	-67	-6	1,185	18	14	1	35
3: Replicate mining boom scenario	-1,365	-1,178	-846	4,856	-258	-70	-70	6
4: Replicate 2011-12 relativities	-208	-193	-142	1,611	-21	1	-8	35
5: Replicate 2010-11 relativities	-332	-287	-224	1,955	-46	-7	-14	29
6: Relativities return to 10-year average	-1,198	-1,009	-744	4,360	-220	-58	-60	2

Sources: Pallas (2021: 185); Victorian Department of Treasury and Finance.

What should Victoria be doing about this?

Victorians should be outraged at the changes which were made to the GST revenue sharing arrangements in 2018, and at the trashing of the principles which have underpinned the distribution of 'general revenue' grants and, subsequently, revenue from the GST, for forty years, in order to appease the greed of what has become the richest state in Australia.

The Victorian Government should never have agreed to them at the time when they were proposed.

All Australian taxpayers – including those living in Victoria – should be appalled that the Commonwealth Government will be incurring more debt (to be serviced, and ultimately repaid, by future generations of Australian taxpayers) in order to transfer billions of dollars to the government of the richest state in Australia, the only government in Australia (and one of very few anywhere in the world) which is currently running, and expects for the foreseeable future to be running, budget surpluses.

There are three things which the Victorian Government, ideally in conjunction with the governments of other eastern states and territories, could and should be doing:

- first, the Victorian and other Governments should be calling for the 2018 changes to be re-visited in light of their significantly greater cost to the Commonwealth than envisaged at the time, especially having regard to the fact that the Commonwealth's financial position is now significantly worse than had been foreseen at the time;
- second, if the Commonwealth is unwilling to agree to the foregoing, the Victorian and other Governments should be insisting that the 'transitional guarantee' that no state or territory will be worse off than they would have been had the 2018 changes not been made be extended beyond the end of the 2026-27 financial year (when it is currently set to expire); and
- third, the Victorian and other Governments should insist on having input into the terms of reference of the proposed review by the Productivity Commission of the altered GST revenue-sharing arrangements in 2026, so as to ensure that they are not 'loaded' towards producing an outcome in favour of Western Australia as was the case with the previous inquiry.

More broadly, given the prospect that Victoria's 'fiscal capacity' may continue to decline relative to that of other states and territories – especially if Victoria is unable to attract the same population flows from the rest of Australia and from overseas as it had been in the years leading up to the onset of Covid-19, or alternatively is unable to find some other 'engine' of economic growth – then Victoria should re-consider its previous long-standing advocacy of a shift to an 'equal per capita' distribution of GST revenues. Such a position may no longer be consistent with Victoria's longer-term interests.

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