

## 6.2 COMMONWEALTH/STATE FINANCIAL RELATIONS

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### Introduction

This Chapter outlines developments in the ACT's financial relations with the Commonwealth, States and the Northern Territory that occurred in 1999-2000. The likely flow-on effects into 2000-01 and possible developments in the outyears have also been identified.

The environment of Commonwealth-State financial relations is set to change dramatically from 1 July 2000 due to the implementation of the Goods and Services Tax (GST), endorsed by all State and Territory leaders who signed a revised *Intergovernmental Agreement on the Reform of Commonwealth-State Financial Relations* (IGA) following the last Premiers' Conference in mid-1999.

The major change in Commonwealth funding arrangements arising from the new taxation regime is that all of the GST revenue will be passed to the States and Territories, replacing Financial Assistance Grants (FAGs) as the major component of Commonwealth funding. This will be conditional on the States abolishing a number of own source taxes and funding a First Home Owners Scheme. The principles and methods underpinning the ACT's share of the GST are also highlighted in this Chapter.

### Overview

Overall, the ACT's immediate and longer term outlook for increases in Commonwealth assistance is highly favourable. With Commonwealth funding accounting for approximately 44.2% of the ACT's General Government Sector revenues, this stream of funding is unlikely to deteriorate given the continued adoption of the Commonwealth Grants Commission's 1999 Review methodology for the next three years, which will see the ACT receiving more than an equal per capita share of the GST revenues. Furthermore, this positive outlook can be expected to continue while ACT economic growth remains steady and generally in line with the national rate.

Importantly, the ACT also stands to benefit much earlier from the implementation of tax reform than most other jurisdictions, thereby enhancing the prospects of future governments' capacity to deliver public services in the Territory.

### Major Developments in 1999-2000

The more notable successes translating into additional Commonwealth funding to the ACT arose from:

- a positive change to the ACT's share of the GST pool to be distributed to the States and Territories in 2000-01; and
- a number of important decisions underpinning National Tax Reform and the consequential change in Commonwealth-State financial relations taken at the Ministerial Council for Commonwealth-State Financial Relations, including:
  - the Commonwealth reiterating its commitment that no State or Territory's budget will be worse off as a result of the changes; and
  - the Commonwealth confirming its commitment to ensuring future Specific Purpose Payment funding aggregates will be maintained.

These factors translate into a gross increase in total general revenue assistance to the ACT of +\$169.3m in 2000-01 above that expected in 1999-2000. However, when the effects of other tax reform measures are included, the net increase is +\$29.9m or 8.2% in nominal terms.

These outcomes and the reasons behind the increases are discussed below in more detail.

### *Increase in the ACT's Commonwealth Grants Commission Recommended Relativity*

The recommendations from the *Commonwealth Grants Commission's 2000 Update Report on General Revenue Grant Relativities*, released on 29 February 2000, improved the ACT's financial position substantially relative to the recommendations contained in the 1999 Review. The Territory's FAGs relativity increased from 1.10270 to 1.14522.

The results of the 2000 Update are of particular importance, given the new taxation arrangements. This is due to the requirement for the Commission to provide a second set of relativities (GST relativities) to be used to distribute the pool of GST revenues to the States and Territories from 1 July 2000.

Although the GST relativities recommended by the 2000 Update were calculated in much the same manner as the FAGs relativities, the two differ because the GST relativities take account of the new arrangements flowing from tax reform. These result in the ACT's GST relativity of 1.11289 being lower than the Territory's FAGs relativity of 1.14522.

Those States with FAGs relativities above one (indicating a greater than equal per capita share of funding) experienced reduced GST relativities that moved them closer to the Australian average. Similarly, those States with FAGs relativities below average experienced an upward move in their GST relativity closer to the Australian average.

This is reflective of a higher average per capita assistance figure being incorporated into the GST relativity compared to the FAGs relativity as a result of the GST pool being substantially larger than the FAGs pool. The GST relativities have thus, necessarily, moved all jurisdictions' relativities closer to the Australian average.

## *2000 Ministerial Council for Commonwealth-State Financial Relations Outcome*

The inaugural meeting of the Ministerial Council for Commonwealth-State Financial Relations took place in Canberra on 17 March 2000.

The Council, which comprises the Commonwealth Treasurer (Chair) and the Treasurers of the States and Territories, replaces the annual Premiers' Conference as the forum for the discussion of matters relating to Commonwealth-State financial relations. The Council deliberated upon a number of topics underpinning the new environment of Commonwealth-State financial relations as well as a range of GST administration issues. However, the most important outcome from the meeting was the Council's decision to approve the estimates contained in the Statement of Estimated Payments (SOEP).

The SOEP provides an outline of the estimated total Commonwealth payments that the States and Territories can expect to receive in 2000-01 when the new taxation reform arrangements are implemented. In effect, the SOEP replaces the former "Offer Document" in the new post Premiers' Conference era.

Additionally, to ensure the agreement of all States and Territories to the national taxation reforms, the Commonwealth undertook that no State or Territory's budgetary position would be worse off as a result of these changes. The underlying rationale for the guarantee was that the size of the GST pool in the early years of the GST is projected to be less than a combination of the State/Territory revenues and grants forgone and the additional expenditures incurred by the States and Territories under the new taxation regime. Over time, national economic growth is projected to increase the size of the GST pool so that all States and Territories will be in a better position than under the current FAGs regime.

In order to give effect to its guarantee, the Commonwealth has put in place a process to provide jurisdictions with a 'top up' to restore their financial positions back to the level they would have been had the reforms to the tax system not been implemented. The amounts of these payments, as well as the methodology used to derive them, were also approved by the Council.

The States and Territories sought assurances from the Commonwealth regarding the level of specific purpose payments (SPPs) in 2000-01, including that the Commonwealth honour the commitment in the Intergovernmental Agreement not to cut aggregate SPPs as part of the tax reform process. The Commonwealth reaffirmed this commitment at the Ministerial Council meeting.

Additionally, the Council considered a range of other topics including:

- a progress report by the GST Administration Sub-Committee (GSTAS);
- the level of Local Government compliance with the GST;
- a report on progress with implementing the First Home Owners Scheme (FHOS); and

- an agreement that the target date for implementing the National Tax Equivalent Regime (NTER) for income tax for State and Territory government business enterprises be deferred from 1 July 2000 to 1 July 2001 and that the remainder of the reciprocal taxation agenda (ie, the application of specified State and Territory taxes to the Commonwealth) be pursued once the NTER is implemented.

### **Commonwealth Grant Funding 1999-2000 to 2003-04**

Table 6.2.1. summarises Commonwealth grant funding to the ACT in 1999-2000, 2000-01 and the forward years arising from the outcomes of the 2000 Ministerial Council for Commonwealth-State Financial Relations.

**Table 6.2.1**  
**Commonwealth Grant Funding to the ACT**

| Payment   | 1999-00 <sup>1</sup> | 2000-01       | Var          | Var         | 2001-02         | 2002-03         | 2003-04         |
|---|----------------------|---------------|--------------|-------------|-----------------|-----------------|-----------------|
|   | Est. Out.<br>\$m     | Budget<br>\$m | \$m          | %           | Estimate<br>\$m | Estimate<br>\$m | Estimate<br>\$m |
| <b>Financial Assistance Grants</b> <sup>2</sup>       | 343.8                | -373.2        | 29.4         | 8.6         | -403.1          | -425.6          | -444.7          |
| <b>GST Revenue Grants</b>                             | n/a                  | 473.5         | n/a          | n/a         | 565.4           | 590.2           | 628.5           |
| <b>Sub Total</b> <sup>3</sup>                         | 343.8                | 473.5         | 129.7        | 37.7        | 565.4           | 590.2           | 628.5           |
| <b>Plus Budget Balancing Assistance:</b>              |                      |               |              |             |                 |                 |                 |
| Budget Balancing Assistance – Grant                   | n/a                  | 16.6          | n/a          | n/a         | 36.6            | 20.2            | 1.4             |
| Budget Balancing Assistance – Loan                    | n/a                  | 22.4          | n/a          | n/a         | 0.0             | 0.0             | 0.0             |
| <b>Budget Balancing Assistance (BBA)</b> <sup>4</sup> | n/a                  | 39.0          | n/a          | n/a         | 36.6            | 20.2            | 1.4             |
| <b>Equals Guaranteed Minimum Amount</b>               | 343.8                | 512.5         | 168.7        | 49.1        | 602.0           | 610.5           | 629.8           |
| <b>Plus Transitional Allowances:</b>                  |                      |               |              |             |                 |                 |                 |
| Police  | 9.3                  | 9.5           | 0.2          | 2.2         | 9.5             | 9.5             | 9.5             |
| <b>Net Transitional Allowances</b>                    | 9.3                  | 9.5           | 0.2          | 2.2         | 9.5             | 9.5             | 9.5             |
| <b>Plus Special Fiscal Needs:</b>                     |                      |               |              |             |                 |                 |                 |
| Family law matters                                    | 0.2                  | 0.2           | 0.0          | 0.0         | 0.2             | 0.2             | 0.2             |
| Corporate affairs compensation                        | 3.7                  | 3.8           | 0.1          | 2.7         | 3.8             | 3.8             | 3.8             |
| <b>Net Special Fiscal Needs</b>                       | 3.9                  | 4.0           | 0.1          | 2.6         | 4.0             | 4.0             | 4.0             |
| <b>Plus National Competition Payments</b>             | 7.2                  | 7.5           | 0.3          | 2.8         | 11.6            | 11.9            | 12.2            |
| <b>Total General Revenue Assistance</b>               | <b>364.2</b>         | <b>533.5</b>  | <b>169.3</b> | <b>46.5</b> | <b>627.1</b>    | <b>635.9</b>    | <b>655.5</b>    |
| <b>Plus Specific Purpose Payments:</b>                |                      |               |              |             |                 |                 |                 |
| Health (includes HCGs)                                | 85.8                 | 88.8          | 3.1          | 3.6         | 92.5            | 97.4            | 103.3           |
| Social Security and Welfare                           | 14.6                 | 16.3          | 1.6          | 11.2        | 18.0            | 19.0            | 19.0            |
| Education   | 86.1                 | 89.4          | 3.4          | 3.9         | 92.8            | 96.3            | 96.3            |
| Public Order and Safety                               | 3.0                  | 3.0           | 0.0          | 1.1         | 3.1             | 3.1             | 3.1             |
| Housing   | 19.2                 | 25.0          | 5.7          | 29.9        | 24.8            | 24.7            | 18.8            |
| Local Govt  | 46.9                 | 48.2          | 1.3          | 2.8         | 49.5            | 50.7            | 51.6            |
| Other   | 33.4                 | 13.0          | -20.4        | -61.2       | 12.5            | 20.7            | 10.9            |
| <b>Total Specific Purpose Payments</b>                | <b>289.0</b>         | <b>283.7</b>  | <b>-5.3</b>  | <b>-1.8</b> | <b>293.2</b>    | <b>311.9</b>    | <b>303.0</b>    |
| <b>Plus Other Commonwealth Payments</b>               |                      |               |              |             |                 |                 |                 |
| Vocational Education and Training                     | 17.4                 | 17.6          | 0.2          | 1.2         | 18.0            | 18.4            | 18.4            |
| Other   | 6.0                  | 5.9           | -0.1         | -1.7        | 5.4             | 5.5             | 5.2             |
| <b>Total Other Commonwealth Payments</b>              | <b>23.5</b>          | <b>23.6</b>   | <b>0.1</b>   | <b>0.4</b>  | <b>23.4</b>     | <b>23.9</b>     | <b>23.6</b>     |
| <b>Total Commonwealth Funding</b>                     | <b>676.6</b>         | <b>840.8</b>  | <b>164.1</b> | <b>24.3</b> | <b>943.7</b>    | <b>971.6</b>    | <b>982.1</b>    |

<sup>1</sup> The 1999-2000 estimated outcome reflects the Commonwealth's latest estimates provided at the Ministerial Council for Commonwealth-State Financial Relations.

<sup>2</sup> Where the FAGs estimates are negative, they have been replaced by GST Revenue Grants (from 2000-01 onwards) reflecting the funding that the ACT would be expected to receive if tax reform had not been implemented. For comparative purposes, the estimated variations of \$29.4m and 8.6% between the 1999-2000 and 2000-01 FAGs have been incorporated (premised on FAGs continuing in 2000-01).

<sup>3</sup> The sub total estimate relates to FAGs in 1999-2000 and GST Revenue Grants in 2000-01 and beyond.

<sup>4</sup> Additional payments made to the ACT to allow the Territory to be no worse off due to effects of national tax reform.

Note: Totals may not add due to rounding.

The variation arises of \$164.1m in Commonwealth funding between 1999-2000 and 2000-01 from the implementation of national tax reform and specifically, the changeover from a FAGs basis to one based on a share of the GST revenue take.

To allow a meaningful comparison between 1999-2000 and 2000-01, total Commonwealth funding needs to be offset by the overall *State Budget Impact* of the total national tax reform package. This is demonstrated below in Table 6.2.2.

**Table 6.2.2**  
**Estimated Impact of Tax Reform on the ACT Budget**

|   | 1999-2000    | 2000-01      | Var          | Var         | 2001-02      | 2002-03      | 2003-04      |
|---|--------------|--------------|--------------|-------------|--------------|--------------|--------------|
|   | Est. Out.    | Budget       |              |             | Estimate     | Estimate     | Estimate     |
|   | \$m          | \$m          | \$m          | %           | \$m          | \$m          | \$m          |
| <b>Total General Revenue Assistance</b>         | <b>364.2</b> | <b>533.5</b> | <b>169.3</b> | <b>46.5</b> | <b>627.1</b> | <b>635.9</b> | <b>655.5</b> |
| <i>Minus</i> <b>State Budget Impacts (SBIs)</b> | n/a          | 139.4        | n/a          | n/a         | 198.9        | 184.8        | 185.1        |
| <b>Total GRA (Minus SBIs)</b>                   | <b>364.2</b> | <b>394.1</b> | <b>29.9</b>  | <b>8.2%</b> | <b>428.2</b> | <b>451.1</b> | <b>470.4</b> |

### *State Budget Impacts (SBIs)*

State Budget Impacts (SBIs) provide an estimate of the net impact on the ACT of changes to the Territory's sources of revenue and expenditure responsibilities. All parties to the IGA have agreed to these estimates.

They also allow for comparisons to be made between the years affected by tax reform and 1999-2000 as they place estimates on like terms. The components that make up the SBIs and the total SBIs for each financial year are provided in the table below.

**Table 6.2.3**  
**Calculation of the ACT's State Budget Impacts**

|  | 2000-01 | 2001-02 | 2002-03 | 2003-04 |
|--|---------|---------|---------|---------|
|  | \$m     | \$m     | \$m     | \$m     |
| Section 90 Revenue Replacement Payments (former Business Franchise Fees) | 97.9    | 106.6   | 110.9   | 115.4   |
| Financial Institutions Duty  | n/a     | 17.4    | 19.5    | 20.0    |
| Marketable Securities Duty   | n/a     | 21.6    | 24.2    | 24.8    |
| Marketable Securities Duty – Remaining Needs adjustment                  | n/a     | -4.0    | -4.2    | -4.5    |
| Reduced gambling revenues  | 16.4    | 18.4    | 18.8    | 19.3    |
| Interest costs   | 1.2     | 0.4     | 0.5     | n/a     |
| Loan repayment   | 0.0     | 22.4    | 0.0     | 0.0     |
| FHOS payments  | 16.5    | 16.8    | 17.1    | 17.5    |
| GST administration costs   | 13.2    | 6.1     | 6.0     | 5.9     |

|   |              |              |              |              |
|---|--------------|--------------|--------------|--------------|
| WST payments  | 4.0          | 4.0          | 4.0          | n/a          |
| OffRoad Diesel Subsidies                            | -0.0         | -0.0         | -0.1         | -0.1         |
| Savings from Tax Reform (abolition of embedded WST) | -8.5         | -9.0         | -9.5         | -10.1        |
| Growth Dividend (State taxes)                       | -1.3         | -1.8         | -2.4         | -3.1         |
| <b>TOTAL State Budget Impact</b>                    | <b>139.4</b> | <b>198.9</b> | <b>184.8</b> | <b>185.1</b> |

The SBIs increase by \$59.5m, or 42.7%, between 2000-01 and 2001-02 due mainly to the proposed abolition of Financial Institutions Duty and Stamp Duty on quoted marketable securities- together with the inclusion of the repayment of the loan component of the ACT's 2000-01 Budget Balancing Assistance. Additionally, the Marketable Securities Duty – Remaining Needs Adjustment also adds to the impact on the ACT budgetary position. The SBIs then stabilise in the outyears.

Although the SBIs generally increase in magnitude from year to year, these increases are more than offset by the growth in GST revenue grants. In the future, however, the SBIs can be expected to increase if the Ministerial Council on Commonwealth-State Financial Relations agrees to the abolition of a number of States taxes required to be reviewed by 2005.

### *Financial Assistance Grants (FAGs)*

The major change in Commonwealth funding to the States and Territories arising from the reforms of the taxation system is that FAGs will be replaced by GST Revenue Grants as the major component of Commonwealth grants from 1 July 2000.

However, a notional FAGs distribution will continue to be derived as part of the calculation of the Guaranteed Minimum Amount (GMA) agreement which is designed to ensure that the ACT's financial position will be no worse off than it would have been had the arrangements for tax reform not been implemented. The derivation of the ACT's GMA is outlined in general terms in the discussion of the ACT's Budget Balancing Assistance below.

The Grants Commission will continue to recommend annual FAGs relativities to be used to estimate what the distribution of FAGs would have been to each State and Territory had the taxation reforms not taken place. To achieve this, from the 2000 Update onwards, the FAGs relativities calculated by the Commission are required to reflect pre-GST arrangements.

Therefore, when calculating the notional FAGs pool, it is necessary for the Commission to unwind all of the GST arrangements and restore them to their FAGs equivalent. This can be achieved by the Commission assessing estimates of the state tax revenue forgone as determined by the Commonwealth Treasury and agreed to by all States and Territories in advance of the GST implementation date of 1 July 2000.

Once derived, the FAGs relativities are applied to a notional FAGs pool that will be estimated annually by the Commonwealth Treasury.

## GST Revenue Grants

The GST revenues will be distributed amongst States and Territories in accordance with Horizontal Fiscal Equalisation (HFE) principles subject to transitional arrangements. That is, the GST revenue will be distributed using the Grants Commission's recommendations of per capita relativities. These recommendations will continue to be assessed on the principles of HFE, reflecting a State or Territory's needs to provide an average level of government services to its residents.

The GST relativities used to distribute GST revenue grants are required to take account of the new arrangements flowing from tax reform. For the first year of the reform process, the Commonwealth Grants Commission was required to reflect in its calculation of the 2000 Update relativity, the following changed arrangements as highlighted in Table 6.2.4:

**Table 6.2.4**

**State and Territory Taxes and Expenditures Affected by the Intergovernmental Agreement on the Reform of Commonwealth-State Financial Relations in 2000-01**

|   |  |
|---|--|
| <p><i>Revenues forgone by the States</i></p> <ul style="list-style-type: none"> <li>• Financial Assistance Grants</li> <li>• Revenue Replacement Payments</li> <li>• Accommodation Taxes (Bed Taxes)</li> <li>• WST Payments by GBEs</li> </ul> | <p><i>Additional costs incurred by the States</i></p> <ul style="list-style-type: none"> <li>• Interest Costs</li> </ul>   |
| <p><i>Reduced expenditures by the States</i></p> <ul style="list-style-type: none"> <li>• Off-Road Diesel Subsidies</li> <li>• Growth Dividend</li> <li>• Savings from Indirect Tax Reform</li> </ul>   | <p><i>Additional expenditures of the States</i></p> <ul style="list-style-type: none"> <li>• First Home Owners Scheme</li> <li>• GST Administration Costs</li> </ul> <p><i>Reduced revenues to the States</i></p> <ul style="list-style-type: none"> <li>• Gambling Taxes</li> </ul> |

The Commonwealth Treasury provided revenue and cost estimates for the above components to the Commission based, as previously stated, on a set of principles agreed by Heads of Treasuries.

For future years, the Commission will also be required to backcast the effects of tax reform arrangements into their assessment of GST relativities, to ensure that the latest assessed relativities reflect the major changes in Commonwealth-State financial arrangements. Future steps in the implementation of tax reform are set out in Table 6.2.5 together with the indicative dates.

**Table 6.2.5**

**Indirect Taxes Affected by the Intergovernmental Agreement on the Reform of Commonwealth-State Financial Relations**

***Abolished from 1 July 2001***

- Financial Institutions Duty
- Stamp Duty on Marketable Securities quoted on the ASX or other recognised exchanges

***Abolished by 1 July 2005, subject to review by the Ministerial Council***

- Debits Tax

***The Ministerial Council to review the need to retain the following by 2005***

- Stamp Duty on non-residential Conveyances
- Stamp Duty on Marketable Securities (unlisted)
- Stamp Duty on Leases
- Stamp Duty on Mortgages, Bonds, Debentures and Other Loan Securities
- Stamp Duty on Credit Arrangements, Instalment Purchase Agreements and Rental Arrangements
- Stamp Duty on Cheques, Bills of Exchange and Promissory Notes

The ACT's inaugural GST relativity of **1.11289** provides for an above per capita distribution to the Territory. When applied to the GST funding pool, the ACT is expected to receive GST revenue totalling \$473.5m in 2000-01.

### ***Guaranteed Minimum Amount/Budget Balancing Assistance***

Heads of Treasuries have agreed to a set of estimates which reflect each State and Territory's financial position in the absence of the reforms to the taxation system being implemented. This notional pre tax reform position is called the *Guaranteed Minimum Amount* (GMA) and equates to the amount of funding that each State or Territory should receive from the Commonwealth to restore its previous position.

The calculation of the GMA incorporates the revenues forgone, including FAGs and the State taxes earmarked for abolition, plus the additional costs that will be imposed as a result of the administration of the GST and the First Home Owners Scheme.

The derivation of the ACT's GMA for 2000-01 is outlined in Table 6.2.6 below, and is covered in more detail at the end of this Chapter.

**Table 6.2.6**

**Calculation of the ACT's Guaranteed Minimum Amount for 2000-01**

| <b>2000-01</b>                      | <b>\$m</b> |
|-------------------------------------|------------|
| <b>State revenue forgone</b>        |            |
| - Financial Assistance Grants       | 373.2      |
| - Revenue Replacement Payments      | 97.9       |
| <b>plus Reduced revenues</b>        |            |
| - Gambling Taxes                    | 16.4       |
| <b>plus Interest costs</b>          |            |
| - Interest Costs                    | 1.2        |
| <b>plus Additional expenditures</b> |            |
| - First Home Owners' Scheme         | 16.5       |

|  |              |
|--|--------------|
| - GST Administration Costs                     | 13.2         |
| <b>plus Other items</b>                        |              |
| - WST Payments                                 | 4.0          |
| <b>minus Reduced expenditures</b>              |              |
| - Savings from Indirect Tax Reform             | 8.5          |
| <b>minus Growth dividend</b>                   |              |
| - Remaining State Taxes                        | 1.3          |
| <b>ACT's Guaranteed Minimum Amount 2000-01</b> | <b>512.5</b> |

Because the ACT's entitlement to GST revenue in 2000-01 falls short of the Territory's GMA, the Commonwealth will provide 'top up' funding to the Territory to allow its financial position to reach this minimum amount. This amount is known as Budget Balancing Assistance (BBA). The ACT's BBA entitlement for 2000-01 is +\$39.0m as illustrated below in Table 6.2.7.

**Table 6.2.7**

**Calculation of the ACT's Budget Balancing Assistance for 2000-01**

|  |                                 | \$m         |
|--|---------------------------------|-------------|
|  | ACT's Guaranteed Minimum Amount | 512.5       |
| <i>minus</i>   | GST Revenue                     | 473.5       |
| <b>Total ACT Budget Balancing Assistance 2000-01</b> |                                 | <b>39.0</b> |

In 2000-01, this +\$39.0m 'top up' payment to the Territory has been determined by the Commonwealth in two parts:

- a grant of \$16.6m attributable to the effects of the Democrats' changes to the original Australian National Tax System (ANTS) tax reform package; and
- an interest free loan of \$22.4m attributable to normal CPI and population parameter changes.

Each year thereafter, each jurisdiction will receive its BBA entitlement, if required, in the form of an annual grant only. Importantly, under the guarantee arrangements, the ACT's GMA calculations for 2001-02 will incorporate Commonwealth funding to repay the loan allowing the Territory to be no worse off.

After the second year following the introduction of the GST, any State or Territory which is receiving more than it would have received under the current arrangements will retain that extra funding. The ACT is one of the jurisdictions to benefit earliest from the new tax arrangements, and on current estimates, will be better off by approximately +\$14.2m in 2004-05 (the first year that the ACT gains from the new arrangements).

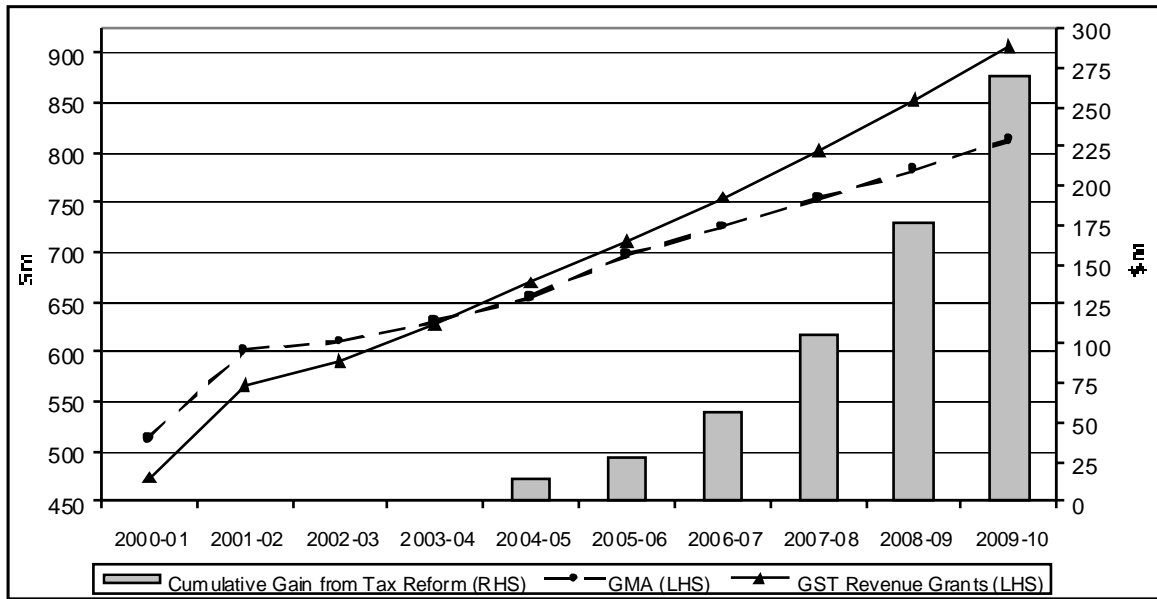
The ACT benefits from the new taxation arrangements sooner than many other jurisdictions because several of the Commonwealth Grants Commission's unfavourable assessments of various State taxes are to be abolished. That is, the ACT is assessed as having a higher than average revenue raising capacity (a lower requirement for financial assistance) in the majority of the State taxes due to be abolished or wound back, and once these State taxes are removed, the ACT's share of financial assistance increases.

This is enhanced by the fact that the ACT's tax raising effort in the majority of the forgone taxes is below the national average. In other words, the ACT has not relied as heavily as most other States in raising revenue from these taxes, and will thus not be affected financially to the same degree when these taxes are abolished.

The following chart highlights the post guarantee benefits to the ACT from tax reform.

Figure 6.2.1

**Estimated Impact of Tax Reform on the ACT – as agreed at the 2000 Ministerial Council for Commonwealth-State Financial Relations**



The above chart illustrates that between 2000-01 to 2003-04, the ACT's GST revenue grants are lower than the GMA calculation (left hand scale). During this period the Commonwealth has undertaken to make up the difference thereby allowing the ACT to be not financially disadvantaged.

By 2004-05, however, the ACT's GST revenue grants are higher than its GMA, with the difference being the financial gains to the Territory. The graph shows the favourable gap growing significantly between 2004-05 to 2009-10. The bar chart, which refers to the right hand scale, shows the cumulative magnitude of the gains. By 2009-10, the accumulated gains to the ACT are estimated to total approximately \$270m.

In the first 10 years the ACT is thus estimated to benefit from the new tax arrangements by nearly \$270m above what it would have received under the old FAGs system if tax reform had not taken place.

The gains identified will allow the ACT to consider further reform of its own tax regime (in conjunction with the other States and the Northern Territory) by abolishing a range of indirect business taxes, such as a range of stamp duties already foreshadowed in the IGA and outlined in Table 6.2.5.

The following table shows the estimated yearly and total impact of tax reform on the ACT as contained in the SOEP, signed at the 2000 Ministerial Council for Commonwealth-State Financial Relations.

**Table 6.2.8**

**Estimated Impact of Tax Reform on the ACT – as agreed at the  
2000 Ministerial Council for Commonwealth-State Financial Relations**

|              | <b>\$m</b>   |
|--------------|--------------|
| 2000-01      | 0.0          |
| 2001-02      | 0.0          |
| 2002-03      | 0.0          |
| 2003-04      | 0.0          |
| 2004-05      | 14.2         |
| 2005-06      | 13.3         |
| 2006-07      | 29.2         |
| 2007-08      | 49.0         |
| 2008-09      | 70.4         |
| 2009-10      | 93.8         |
| <b>TOTAL</b> | <b>269.9</b> |

The above estimates are broadly indicative and are subject to further revision<sup>5</sup>. They are based only on those impact items incorporated in the Guaranteed Minimum Amount calculation. Additionally, the following assumptions were used in their preparation:

- constant annual increases in GST revenue of around 6 % after 2003-04;
- relative stability in Commonwealth Grants Commission assessment of needs; and
- debits tax is abolished from 1 July 2005; and business stamp duties are retained by the States (the Ministerial Council will be reviewing the need for their retention by 2005).

### *Transitional Allowances*

The Commonwealth Grants Commission has assessed transitional allowances for the ACT since 1992 to take account of constraints on the ACT's budget flexibility arising from policies inherited from the Commonwealth at self government in April 1989. Transitional allowances are funded directly by the Commonwealth. They represent unique payments to the ACT and, as such, fall outside the pool of State grants and are not directly related to the relativity process.

The only transitional allowance for 2000-01 comprises \$9.5m for police, an increase over the 1999-2000 figure of \$0.2m, or 2.2%. This is in recognition of the ACT's continuing limited policy control over the provision of police services. The current level of expenditure on policing in the ACT represents the combined effect of lower than average service levels and

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<sup>5</sup> For example, as discussed in Chapter 4.4 *Goods and Services Tax*, current ACT modelling has identified a shortfall in the embedded savings available to the Territory from the abolition of the existing wholesale sales tax (WST) Tax Equivalent Regimes (TER) of \$3.917m in 2000-01 only, compared with the SOEP.

higher than average salaries and salary related payments. While the service levels are capable of limited negotiation with the Commonwealth, the ACT is not able to influence the unit costs.

Given the high costs of salaries and other conditions of employment and the absence of effective policy control over these, the ACT would not be able to provide a standard level of service without incurring substantial above standard costs. The continuance of the transitional allowance is essential to provide the capacity for the ACT to provide a standard level of service.

A related development in this area was the signing on 15 March 2000 of a new Arrangement for the provision of police services to the ACT by the Commonwealth Minister for Justice and Customs and the ACT Attorney-General. Under the new Arrangement, the Australian Federal Police will enter into an annual Purchase Agreement with the ACT Government specifying levels of service to be provided to the community.

Importantly, although the Arrangement represents a step forward for the political ownership of the contract, the Arrangement still specifies that the Commonwealth will retain control over terms and conditions of employment and salary levels in relation to personnel providing policing services.

### *Special Fiscal Needs*

The Commission also recommends funding to the ACT for special fiscal needs to take account of differences in financial arrangements between the Commonwealth and the ACT and the Commonwealth and the States for a number of services. Special fiscal needs will rise by \$0.1m in 2000-01.

### *National Competition Payments*

These payments are to be paid in three tranches, with the first tranche payment having commenced in July 1997. The tranche payments to the States and Territories are \$200m per annum from 1997-98 (first tranche), \$400m per annum from 1999-2000 (second tranche) and \$600m per annum from 2001-02 to 2005-06 (third tranche). The expected funding is expressed in 1994-95 dollars and is escalated annually to account for inflation and distributed amongst the States and Territories on a population share basis. In 2000-01 the Commonwealth is expected to pay the ACT \$7.5m. A detailed discussion on the requirements underpinning these payments is contained in Chapter 6.1 *Economic Conditions*.

### *Specific Purpose Payments*

The signing of a number of SPP agreements has removed a high degree of uncertainty in the ACT's ability to continue jointly funded public programs at current or enhanced levels in the critical fields of housing, tertiary education, health and welfare sectors.

Some of the more notable funding programs either signed or ratified during 1999-2000 included:

- a bilateral Public Health Outcome Funding Agreement securing \$6.378m over two years for public health programs in the ACT; and
- signing of a new Commonwealth-State Housing Agreement.

### *Other Commonwealth Funding*

#### *Vocational Education and Training - Australian National Training Authority (ANTA) Agreement*

Along with the other States and the Northern Territory, the ACT agreed to the revised Australian National Training Authority (ANTA) Multilateral Agreement in December 1997. The Bilateral Agreement was also signed by the ACT in May 1998. The ANTA Agreement provides funding for Vocational Education and Training, with the ACT to receive approximately \$17.4m in 1999-2000.

This agreement will be renegotiated in late 2000.

## Detailed Description and Estimates of the Components of the ACT's Guaranteed Minimum Amount

Due to the importance of the calculations and estimates underpinning the components of the Guaranteed Minimum Amount, already foreshadowed in Table 6.2.6 of this Chapter, a detailed methodological description is set out below in the interests of accountability and transparency in the move to the new tax reform process.

### ACT Revenue Forgone

**Financial Assistance Grants (FAGs)** - FAGs will cease to be paid to States and Territories from 1 July 2000 and are therefore included in the GMA. The CGC will continue to calculate FAGs relativities which will be applied to a notional FAGs pool (estimated by Commonwealth Treasury to reflect growth in the CPI and State populations) to determine the ex-ante and ex-post estimates of FAGs. State-by-State estimates of FAGs will be provided to all jurisdictions by Commonwealth Treasury.

**Business Franchise Fee - Revenue Replacement Payments** - the revenue forgone under this category will be the ACT's revenue replacement payments (RRPs) in respect of petrol, tobacco and alcohol. Adjustments will be made for the difference between estimates and the final payments of safety net collections for the three elements that make up the total business franchise fee revenue replacement payments.

Estimates will be provided by Commonwealth Treasury on the following RRP components.

- *Petrol* - the Commonwealth will provide ex-ante estimates of the ACT's level of revenue forgone for petrol in 2000-01 by indexing the ACT's RRP for petrol in 1999-2000 by the Commonwealth's forecasts of annual growth in total petroleum consumption and adjusted CPI growth. This estimate will also be reduced by the estimated safety net amount the Commonwealth will pay to the ACT in 2000-01 in respect of safety net surcharge liabilities for 1999-2000. Ex-post estimates will reflect the actual level of revenue forgone, observed growth in petrol consumption in the year, adjusted CPI outcomes and the actual safety net amounts paid to the ACT by the Commonwealth in 2000-01. In each subsequent year, the Commonwealth will provide ex-ante estimates determined by indexing the previous year's final estimate by the Commonwealth's forecast of annual growth in total petroleum consumption and adjusted CPI growth.
- *Tobacco* - the Commonwealth will provide ex-ante estimates of the ACT's level of revenue forgone for tobacco in 2000-01 based on the ACT's RRP for tobacco products in 1998-99 adjusted for any differences between the estimate of tobacco safety net collections and the actual tobacco safety net collection for June 1999. These estimates will be indexed by Commonwealth factors that reflect declines in volume and prices growth determined by CPI indexation for tobacco excise. The ex-ante estimates will be subject to an ex-post adjustment that reflects changes to the CPI outcomes. In each subsequent year, the Commonwealth will provide ex-ante estimates determined by indexing the previous year's final estimate by the Commonwealth's indexation factors as described above.
- *Alcohol* - the Commonwealth will provide ex-ante estimates of the ACT's level of revenue forgone for alcohol in 2000-01 by indexing the ACT's RRP for alcohol products in 1999-2000 by Commonwealth forecasts of growth in nominal household final consumption of alcohol. This estimate will also be reduced by the estimated safety net amount the Commonwealth will pay to the ACT in 2000-01 in respect to safety net surcharge liabilities for 1999-2000. Ex-post estimates will reflect the actual level of revenue forgone, observed growth in nominal household final consumption of alcohol and the actual safety net amounts paid to the ACT by the Commonwealth in 2000-01. In each subsequent year, the Commonwealth will provide ex-ante estimates determined by indexing the previous year's final estimate by the Commonwealth's forecasts of nominal household final consumption of alcohol. The ex-ante estimates will be subject to an ex-post adjustment that reflects the observed growth in the nominal household consumption of alcohol.

## PLUS

### State Taxes to Be Abolished

- *Bed Taxes* – this is the only State tax to be abolished on 1 July 2000. NSW and the NT are the only jurisdictions to currently levy this tax and estimates of the revenue forgone have been agreed between those two jurisdictions and the Commonwealth.
- *Financial Institutions Duty (FID)* – the Commonwealth and the States have agreed to cease collecting FID on 1 July 2001. The following estimates for FID have been agreed between the Commonwealth and the States and will remain unchanged for ex-ante and final calculations of the GMA:
  - ACT estimate for 2001-02 is \$17.4m;
  - ACT estimate for 2002-03 is \$19.5m; and
  - ACT estimate for 2003-04 is \$20.0m.
- *Stamp Duty on the Transfer of Marketable Securities* – in accordance with the IGA, the Commonwealth and States have agreed to cease collecting stamp duty on the transfer of listed marketable securities on 1 July 2001. Ex-ante estimates of the revenue forgone have been provided by the States and prepared on the basis that all such duty has been abolished. However, the cessation of this stamp duty applies only to marketable securities quoted on the Australian Stock Exchange or some other recognised exchange. Therefore, ex-post estimates of revenue forgone will include amounts that represent the CGC's calculation of 'needs' contained in a State's share of GST revenue associated with the retention of stamp duty on unquoted marketable securities after 1 July 2001.

## PLUS

### Reduced Revenues

- *Gambling Tax Arrangements* - the IGA requires the ACT to adjust its gambling tax arrangements to take account of the application of the GST to gambling operators. Therefore, the reductions in gambling revenues and the impact on the ACT's budget are included in the GMA. Estimates are to be provided by the States and are subject to change. Ex ante estimates will be based on the ACT's estimate of the full amount of GST revenue to be raised from gambling activity. The final determination of the GMA will be based on the actual relief from the impact of the GST provided by the ACT to gambling operators.

## PLUS

### Interest Costs of Cash Flow Shortfall

- *Interest Costs on Cash Flow Shortfall* - the interest cost incurred by the ACT due to the tax reforms is included in the determination of the GMA. This cost arises from the change to cash flows due to the replacement of weekly payments of FAGs, revenue replacement payments and State and Territory taxes with monthly payments of GST revenue grants and guarantee loans and grants. This cost is only included in the calculation of the GMA for the initial three-year period 2000-01 to 2002-03. The Commonwealth will not compensate the ACT and other States for this cost after the third year. The following ex ante estimates of the interest costs have been agreed between the Commonwealth and the ACT and will remain unchanged for final calculations of the GMA:
  - ACT estimate for 2000-01 is \$1.2m;
  - ACT estimate for 2001-02 is \$0.4m;
  - ACT estimate for 2002-03 is \$0.5m; and
  - ACT estimate for 2003-04 is \$0.0m.

## PLUS

### Loan Repayments

- *Loan Repayments* - in 2001-02 only, the repayment of the guarantee loan of \$22.4m by the ACT will be included in the GMA.

## PLUS

### Additional Expenditures

- *GST Administration Costs* - a requirement of the IGA is that States will be responsible for the administration costs of the GST payable to the Australian Tax Office. Therefore, the additional outlays required by the ACT are included in the determination of the GMA. The ex-ante estimates of GST administration costs will be distributed amongst States and Territories on an equal per capita basis according to ABS population estimates. Ex-post estimates and final payments will reflect the actual amounts paid to the Commonwealth for the administration of the GST.
- *First Home Owners Scheme Costs* - States and Territories are required to fund a First Home Owners Scheme (FHOS) to offset the impact of the GST on the price of new homes. The additional outlays required are also included in the determination of the GMA. The Commonwealth will provide ex-ante estimates of the annual cost of this scheme based on a lump sum payment of \$7,000 per eligible homebuyer. The number of eligible homebuyers will be estimated by using the most recent ABS data on the number of first homeowners in the ACT. This estimate will be projected forward by the Commonwealth's estimates of civilian non-farm wage and salary employment. The final determination of FHOS amounts for the determination of the GMA will be based on the actual payments made by the ACT under its scheme in accordance with the IGA.

## PLUS

### Wholesale Sales Tax (WST) Tax Equivalent Regimes (TER) Payments

- Wholesale Sales Tax (WST) Tax Equivalent Regime (TER) Payments - estimates are to be included in the calculation of the GMA to recognise the revenue forgone by the ACT in relation to the abolition of WST TERs on government owned business operations. Estimates for these revenues forgone have been agreed between the States and the Commonwealth and will remain unchanged for ex ante and final calculations of the GMA.
  - ACT estimate for 2000-01 is \$4.0m;
  - ACT estimate for 2001-02 is \$4.0m;
  - ACT estimate for 2002-03 is \$4.0m; and
  - ACT estimate for 2003-04 is \$0.0m.

## MINUS

### Reduced Expenditures

- *Reduced Costs to Government from Indirect Tax Reform* - the benefits accruing to the ACT from the reduction in embedded taxes on government purchases are to be included in the determination of the GMA. The Commonwealth's PRISMOD model has been used to identify the impact of the indirect tax changes on Government Final Consumption Expenditure (GFCE) and Government Gross Fixed Capital Expenditure (GFKE). The Commonwealth has provided the ACT's ex-ante estimates of reduced costs by estimating the ACT's share of the 'gross expenditure on goods and services' and 'expenditure on new fixed assets components' of GFCE and GFKE respectively. The estimates below have been agreed between the ACT and the Commonwealth and will remain unchanged for ex-ante estimates:
  - ACT estimate for 2000-01 is \$8.5m;
  - ACT estimate for 2001-02 is \$9.0m;
  - ACT estimate for 2002-03 is \$9.5m; and

- ACT estimate for 2003-04 is \$10.1m.
- *State Rebates for Off-Road Diesel* - on 1 July 2000, the ACT will terminate its off-road diesel rebate scheme, and the Commonwealth will amend the Diesel Fuel Rebate scheme to provide rebates for qualified road users. The savings to the ACT are to be included in the GMA. The Commonwealth will provide ex-ante estimates on the level of expenditure forgone determined by the per capita cost to the ACT of its off road diesel subsidies paid in 1999-2000. This amount will be indexed each year in line with the estimates of the ACT's revenue forgone in relation to revenue replacement payments of petrol and then multiplied by the estimated population of the ACT in the relevant year. An ex-post estimate will reflect the ACT's actual forgone RRP's for petrol and ABS population determinations.

**MINUS**

**Growth Dividend**

- *Growth Dividend – Remaining State Taxes* - the growth dividend attributable to remaining State taxes is included in the calculation of the GMA to recognise the higher tax revenues that will flow to the ACT because of the positive impact of tax reform on the Territory's economy. The Commonwealth has provided estimates of the growth dividend attributable to the ACT's remaining State taxes, with the ACT's share determined on the basis of the Territory's estimated share of remaining State tax revenues as agreed with the Commonwealth. These estimates will remain unchanged for the ex-ante and final calculations of the GMA.
  - ACT estimate for 2000-01 is \$1.3m;
  - ACT estimate for 2001-02 is \$1.8m;
  - ACT estimate for 2002-03 is \$2.4m; and
  - ACT estimate for 2003-04 is \$3.1m.

**PLUS**

**Adjustments**

- *Adjustments* - from 2001-02, adjustments will be made to the ACT's GMA to account for the net difference between preliminary estimates and outcomes of final estimates for items that were taken into account for the ACT's GMA in the previous year.

**EQUALS**

**ACT's Guaranteed Minimum Amount**