

# Australian Government Grants

## Overview

Australian Government grants are an important source of revenue for all states. The grants are necessary as, under Australia's federal system, the states have significant service delivery responsibilities but limited capacity to raise own-source revenue, while the Australian Government's revenue-raising capacity exceeds its limited responsibility for providing services. The mismatch between the revenue powers and service delivery responsibilities of the Australian and state governments is described as vertical fiscal imbalance and has increased following the tax reforms associated with the introduction of goods and services tax (GST) and the abolition of a range of state taxes.

There are two types of Australian Government grants to states:

- general purpose grants, which include GST revenue payments and, in the case of the Territory, grants in lieu of uranium royalties, and national competition payments (final payment in 2005-06). These are untied payments that can be used by the states for any purpose; and
- other grants. The majority of these are classified by the Australian Government as specific purpose payments (SPPs) and are earmarked for specific purposes and represent tied funding.

The table below highlights the importance of Australian Government grants to the states and the Northern Territory in particular. These numbers differ slightly from the Territory's budget estimates to allow comparison across jurisdictions.

Table 5.1: Sources of Revenue for the Northern Territory and All States in 2006-07

	Northern Territory % of total revenue	All states % of total revenue
General purpose payments <sup>1</sup>	69.9	28.2
Specific purpose payments <sup>2</sup>	14.7	19.7
Own-source revenue	15.4	52.1
<b>Total</b>	<b>100.0</b>	<b>100.0</b>

<sup>1</sup> GST and grants in lieu of uranium royalties.

<sup>2</sup> Includes SPPs 'to' and 'through' the states.

Sources: Statement of Estimated Payments to the States and Territories, 30 March 2006; state and territory 2005-06 mid-year reports.

The Northern Territory is much more reliant on Australian Government grants than other states, with around 85 per cent of its revenue sourced from the Australian Government. In other states, Australian Government grants account for around 50 per cent of revenues. This greater reliance on Australian Government grants reflects the higher cost and demand for government services and the low revenue-raising capacity of the Territory relative to other states.

## Intergovernmental Agreement

The June 1999 Intergovernmental Agreement on the Reform of Commonwealth-State Financial Relations (the Intergovernmental Agreement) defines the principles and institutional arrangements by which the Australian Government collects GST revenue on behalf of the states and territories (hereafter referred to as the states). Since its implementation in July 2000, the Intergovernmental Agreement has been the centrepiece of financial relations between the two levels of government.

The Australian Government has collected revenue on behalf of the states since the 1940s, when the states' income taxation powers were transferred to the Australian Government. Prior to the Intergovernmental Agreement, the amount of federal taxation revenue passed on to the states was at the discretion of the Australian Government. Competing budget pressures and policy priorities had resulted in a decreasing share of Australian Government revenue, particularly untied revenue, being passed on to the states over time.

By the 1990s, financial arrangements between the two levels of government were both inefficient and becoming unsustainable. The cost of providing state services, particularly health and law and order, was growing faster than revenue from the Australian Government. At the same time, the relative importance of state own-source revenue was increasing as the states sought to fund the increasing demand for, and costs of, government services.

The primary objectives of the tax reforms introduced under the Intergovernmental Agreement were:

- to guarantee states access to a source of untied revenue which would, over time, better align with growth in the cost of state services;
- to allow for the staged abolition of a specified list of state taxes; and
- to simplify financial relations between the Australian Government and the states.

Under the Intergovernmental Agreement, all GST revenue is provided to the states and distributed in accordance with the principle of horizontal fiscal equalisation.

The Intergovernmental Agreement requires the states to:

- forgo financial assistance grants, which provided the bulk of untied grants to the states before the introduction of the GST;
- abolish a range of their own taxes, including financial institutions duty, stamp duty on shares and marketable securities and bed taxes; and
- review by 2005 the need to maintain a number of other taxes.

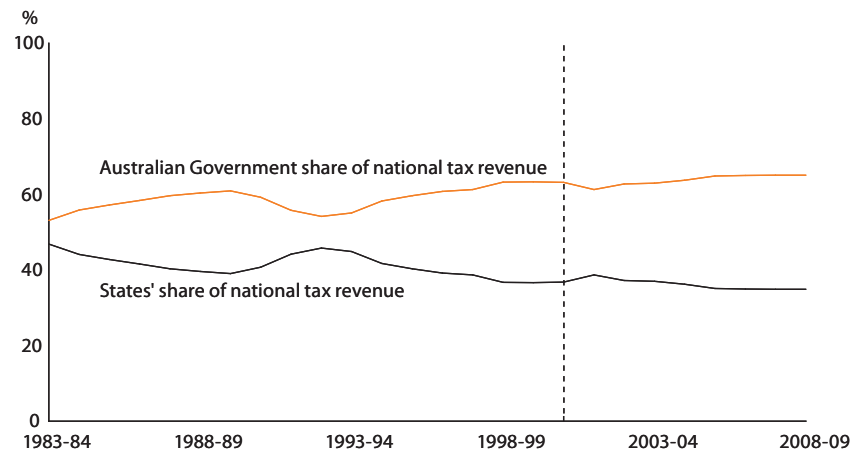
A key feature of the Intergovernmental Agreement is a guarantee that no state will be financially disadvantaged by the tax reforms introduced in 2000. To satisfy that commitment, the Australian Government agreed to provide budget balancing assistance (BBA) to offset the revenue shortfall for as long as any state is worse off than under previous funding arrangements. Following a decision by the majority of states to abolish a number of business-related stamp duties that were subject to review under the Intergovernmental Agreement, the Australian Government has conditionally agreed to extend the transitional arrangements to 2008-09.

In aggregate, the states are expected to be \$1.1 billion better off in 2005-06 than they would have been without tax reform, however the impact of tax reform on states has varied. Most states (including the Territory) have experienced higher funding levels than previous funding arrangements for a number of years, while other states have yet to receive any significant benefits. The positive result for most states is largely due to the benefits of higher than expected growth in GST revenue, due to robust economic conditions and a low inflationary environment, that has provided strong growth in all government revenues. However, the growth in GST revenue has not been sufficient to correct a continuing decline in the states' share of national tax revenue.



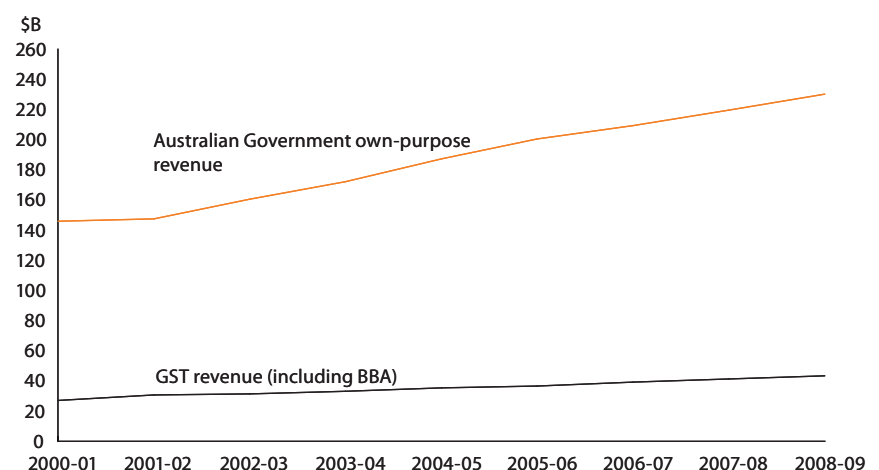
Chart 5.1 illustrates the continuation of a long-term trend decline in the states' share of national revenue, including state own-source revenue, after the introduction of the GST in 2000. Although the GST has grown strongly since 2000, the relative strength and size of the Australian Government tax base ensures that the proportion of national revenue assigned to state purposes continues to reduce. In 1983-84, nearly half of national revenue was dedicated to state services. On current forward estimates, this proportion will have fallen to about 35 per cent by 2008-09.

Chart 5.1: State and Territory Share of National Taxation Revenue



Although the GST revenue passed to the states has grown more strongly than expected since 2000, Australian Government revenues have also increased significantly. Based on 2005-06 projections, Australian Government own-purpose revenue will have grown by more than \$50 billion since the GST was introduced (see Chart 5.2) and at a higher rate than GST. As a result, the Australian Government's projected cash surplus of \$11.5 billion in 2005-06 is greater than the accumulated benefit of the GST to all states and territories since 2000, and around a third of total GST revenue passed on to the states in 2005-06.

Chart 5.2: Growth in Australian Government Revenue



The Intergovernmental Agreement provided for an annual meeting of all Australian Treasurers, known as the Treasurers' Conference, to oversee its operation. The seventh annual Treasurers' Conference was convened on 31 March 2006. The main agenda item at the meeting was the states' undertaking in the Intergovernmental Agreement to "review the need" for a range of taxes by 2005.

Prior to the Treasurer's Conference, seven states, excluding New South Wales, responded to the Australian Treasurer's request for states to commence the abolition of taxes listed for review from 1 July 2006. Each state decided on separate timetables for the abolition of a range of stamp duties over five years commencing in 2006-07. The Territory's timetable for abolition spans four years.

The seven states agreed to phase out the business component of non-residential conveyances. States opposed the abolition of stamp duty on non-residential conveyances due to its importance as a source of revenue and inequity with purchasers of residential property, particularly first home buyers.

At the 2006 Treasurer's Conference, the Australian Treasurer agreed to the seven states' timetable for abolishing the taxes listed for review under the Intergovernmental Agreement. However, the Australian Treasurer continues to seek consensus among the states on the abolition of stamp duty on the real property component of non-residential conveyances. To ensure that no state is worse off from the abolition of this tax, the Australian Government has offered to extend the provision of budget balancing assistance to 2008-09.

Subsequent to the Treasurers' Conference, New South Wales has put forward a timetable for the abolition of certain taxes to the Australian Treasurer.

## GST Revenue

The Territory expects to receive \$1829.4 million in GST-related revenue in 2005-06, a 5.2 per cent increase from the \$1739.6 million received in 2004-05. For 2006-07, a stronger increase of 7.6 per cent to \$1967.7 million is expected. The more rapid growth reflects an increased relativity and improved population growth. The Territory's estimates of GST growth for 2005-06 and 2006-07 are marginally lower than those of the Australian Government due to more conservative population growth assumptions.

## Commonwealth Grants Commission

The role of the Commonwealth Grants Commission (hereafter referred to as the Commission) is to advise the Australian Government on relativities for use in the distribution of GST revenue among the states. The Intergovernmental Agreement requires these recommendations to be based on the principle of horizontal fiscal equalisation, which is defined as:

*State governments should receive funding from the pool of goods and services tax revenue and health care grants such that, if each made the same effort to raise revenue from its own sources and operated at the same level of efficiency, each would have the capacity to provide services at the same standard. (Commission 2006 Update Report)*

The Commission's recommendations are expressed in per capita relativities for each state. The relativities represent the relative per capita need of each state for assistance that, together with the revenue from its taxes and charges, would give it financial capacity to provide the national average of government services. They take into account differences in:

- states' expenditure needs, including both the cost of, and demand for, government services; and
- states' capacity to raise own-source revenues.

The relativities are applied to each state's share of national population to calculate weighted population shares or grant shares. These are then applied to the pool of grants to calculate each state's grant level.



Every five years, the Commission undertakes a major review of the method it uses to determine per capita relativities. This process is necessary to ensure that relativities continue to reflect the contemporary public administration, service provision and revenue-raising environment of state governments. The last review was completed in February 2004. The 2004 Review methodology will be used as the basis for determining GST distribution among states to 2009-10. Relativities in the intervening years are updated using the latest available financial, economic and demographic data.

### 2006 Update – State Revenue Sharing Relativities

The Report on State Revenue Sharing Relativities – 2006 Update details the results of the Commission’s latest analysis of data. In its 2006 Update, the Commission recommended an increase in relativities for New South Wales, Victoria, the Australian Capital Territory and the Northern Territory. The remaining jurisdictions experienced a decrease in relativities. The 2006 Update relativities will be used to distribute GST revenue among the states in 2006-07.

The table below shows the change in per capita relativities and each state’s share of GST revenue using the 2005-06 GST pool between the 2005 and 2006 Updates.

Table 5.2: Impact of the 2006 Update

	NSW	Vic	Qld	WA	SA	Tas	ACT	NT
<b>2005 Update</b>								
Relativity	0.86846	0.87552	1.04389	1.02500	1.20325	1.55299	1.14300	4.26682
Population share (%)	33.3	24.7	19.5	9.9	7.6	2.4	1.6	1.0
Grant share (%)	29.1	21.7	20.1	10.1	9.2	3.7	1.9	4.3
<b>2006 Update</b>								
Relativity	0.87332	0.89559	1.02387	1.00480	1.18862	1.54931	1.14575	4.32755
Population share (%)	33.3	24.7	19.5	9.9	7.6	2.4	1.6	1.0
Grant share (%)	29.1	22.1	20.0	10.0	9.0	3.7	1.8	4.3
<b>Impact (\$M)</b>	<b>70.7</b>	<b>220.2</b>	<b>-175.6</b>	<b>-90.0</b>	<b>-49.8</b>	<b>-4.1</b>	<b>1.9</b>	<b>26.7</b>
<b>Impact (\$ per capita)</b>	<b>10.37</b>	<b>43.52</b>	<b>-43.91</b>	<b>-44.30</b>	<b>-32.21</b>	<b>-8.43</b>	<b>5.70</b>	<b>131.27</b>

Source: Commonwealth Grants Commission Report on State Revenue Sharing Relativities – 2006 Update.

The outcome for the Territory was an increase in its relativity from 4.26682 to 4.32755, which translates to a \$26.7 million increase in the Territory’s share of GST revenue based on the 2005-06 GST pool. In per capita terms, the largest positive impacts were in the Northern Territory (\$131.27) and Victoria (\$43.52), while the greatest negative impacts were in Western Australia (-\$44.30) and Queensland (-\$43.91).

In the 2006 Update, the changes to the states’ share of GST revenue were primarily driven by adjustments to the relative revenue-raising capacities of the states, which were heavily influenced by revisions to data and cyclical effects related to the property and mining sectors. The cyclical effects occur over a number of years due to the Commission’s five-year averaging process. The reference years for the 2006 Update are 2000-01 to 2004-05. Changes in the relative costs of providing services were generally of lower magnitude and had offsetting impacts.

The major data change was the Australian Bureau of Statistics' revision to its Compensation of Employees data, resulting in substantial changes to the payroll tax and gambling assessments. This data revision accounted for more than 60 per cent of the total change in redistribution to the Territory in the 2006 Update.

The continued growth in the Queensland and Western Australian property and mining sectors has increased these states' capacity to raise stamp duty on conveyances and mining royalties. Subsequently, these states were assessed as needing a smaller share of the GST revenue in 2006-07 compared with 2005-06. In comparison, the slow down in the property market in New South Wales and Victoria has reduced the revenue-raising capacity of these states, in turn leading to an increased share of GST revenue for these states.

The Commission's recommended relativities are based on assessments of revenue and expenditure needs for each state and territory. The Commission uses the term 'need' to describe the financial effect on each jurisdiction of:

- unavoidable influences on the use or cost of providing services (expenditure needs);
- unavoidable influences on revenue-raising capacities (revenue needs); and
- its per capita level of SPPs in relation to the national average (SPP needs).

In the last year for which the Commission has completed its assessments (2004-05), the Territory was assessed as requiring to spend \$12 480 per capita to provide a standard level of government services, compared with a national average of \$5154 per capita. The difference between these amounts, \$7325 per capita, is the sum of the Territory's assessed per capita expenditure needs.

Needs may be positive or negative. It is a necessary consequence of the Territory's assessed positive expenditure needs that at least one other jurisdiction will be assessed as having negative expenditure needs.

Expenditure needs are assessed by examining factors that influence the costs of, and demand for, services. The high cost of delivering government services in the Territory is mainly due to its small and widely dispersed population, the unique composition of its population, its harsh physical environment and its relative isolation from Australia's main population centres.

Revenue needs result from factors that influence each state's capacity to generate revenue from its own sources. These factors include differences between states in developed natural resource endowments and the divergent structure of state economies. The Territory is assessed as having low revenue-raising capacity relative to other states (about \$2036 per capita compared to the national average of \$2314 in 2004-05) and is therefore assessed as having positive revenue needs.

The third broad component of the Commission's assessment is SPPs. The Territory has negative SPP needs as it receives greater than its per capita share of SPP funding, largely due to programs for Indigenous services.

When all expenditure, revenue and SPP needs are combined to calculate shares of the GST pool, the Territory's share of GST revenue is about 4.3 per cent compared to a per capita share of about 1 per cent. New South Wales and Victoria are the only jurisdictions that will receive less than an equal per capita share of GST revenue in 2006-07, due to their comparative advantages in raising own-source revenue, and lower than average costs of providing services.



## 2010 Review of State Revenue Sharing Relativities – Progress Report to Ministerial Council for Commonwealth-State Financial Relations 2006

The 2010 Review Terms of Reference instructed the Commission to provide a progress report to the Ministerial Council on aspects of the review, including identifying ways to simplify its assessments, eliminating unreliable assessments because of unsatisfactory data or method, and the application of materiality thresholds.

The Commission's report covers five broad issues:

- utilising a top-down approach for assessment;
- imposing materiality thresholds to enhance simplicity;
- dealing with unreliable data;
- early implementation; and
- reviewing horizontal fiscal equalisation (HFE) principles and implementation.

Broadly, the Commission is proposing to approach the 2010 Review with a clean slate by adoption of a top-down approach to assessment with materiality thresholds below which assessments or disabilities that fail to meet these thresholds would be aggregated or treated equal per capita.

Using the clean slate approach, the Commission will start with broad expense and revenue categories which would be disaggregated only if the category meets materiality thresholds, can be measured reliably and improves equalisation outcomes.

The Commission has released draft guidelines for dealing with unreliable data and is implementing programs to improve data quality while proposing to continue its use of judgement where appropriate. The guidelines are designed to achieve consistent and appropriate standards in the assessment of disabilities and development of categories, while ensuring simplicity and transparency.

The Territory has provided cautious support to the top-down approach, subject to equalisation maintaining primacy over simplification, a review of the impact of the thresholds and the continuing use of judgement where data is less reliable. There are significant risks for the Territory to the extent that valid disabilities are discarded simply because they are subjectively judged to be immaterial or data is considered unreliable.

During 2006, the Commission's workplan will focus on the architecture of equalisation, advancing the work on aggregation of categories and examining the reliability of major datasets.

The Commission is promoting debate regarding the principles of HFE and is seeking state submissions in 2006. The Territory supports the Commission's efforts to promote constructive debate regarding HFE and welcomes any review with confidence that the current system has stood the test of time and weathered much criticism.

## Indigenous Related Expenditure and Revenue Review – Preliminary Results

In 2005-06, Northern Territory Treasury commenced a review of the share of Territory expenditure and revenue that is related to its Indigenous population. The study is being carried out in consultation with all Northern Territory general government agencies, which have offered input and endorsement of the analysis and methodologies applied.

The purpose of the review is to offer robust and defensible estimates to respond to recent criticism from various quarters, including other governments and academics, of the Northern Territory Government's expenditure priorities. These critics have argued that the Territory's spending policies have been insufficient to cater for the disadvantages faced by its Indigenous population. It should be noted that these criticisms are largely misplaced in that the bulk of the Territory's revenue (that is, GST) is provided as untied revenue to states, and at a practical level should not be attributed to various population sub-groups. However, the review is worthwhile in the context of funding for programs specifically targeted at Indigenous Territorians and the Commission's data on contributions to redistribution of GST revenue.

The amount of revenue related to the Indigenous population was derived by adding the direct value of specific purpose payments targeted at Indigenous Territorians to the Commission's attribution of redistribution relating to Indigenous influences, native title and land rights and an equal per capita attribution of all other government revenue. Offsetting this amount was the indirect effect contained within the Commission's assessment of relativities relating to specific purpose payments for Indigenous purposes. Preliminary results for this methodology show that about \$1.2 billion, or 44.8 per cent, of the Territory's revenue is related to its Indigenous population.

Expenditure related to the Indigenous population has been estimated on the basis of usage rates and availability of government services and cost differentials in providing services. The analysis was carried out on a sub-output, or program, basis to ensure sufficient detail in service definition.

Agencies were classified according to the nature of the service provided. Service agencies are those providing services directly to the public, support agencies were classified as those representing services to agencies and central agencies provide both service and support functions. The expenditure attributable to the Indigenous population for support agencies and functions was estimated by applying the weighted proportions derived from service agencies or functions. The support functions essentially represent the necessary wheels of government to ensure services can be provided to the population or population sub-groups.

Based on this methodology, preliminary results show that about 48.9 per cent of the Territory's expenditure is related to its Indigenous population. If central agencies were removed from the analysis, the share of the Territory's total expenditure which is related to the Indigenous population increases to 49.7 per cent (Table 5.3).



Table 5.3: Expenditure attributable to the Indigenous population, 2004-05 (preliminary)

	Total Expenditure \$M	Indigenous Attributed Expenditure \$M	Indigenous as % of Total Expenditure %
All General Government Agencies	2 684	1 311	48.9
General Government Agencies excluding central agencies <sup>1</sup>	2 224	1 106	49.7

<sup>1</sup> Central agencies include the Department of the Chief Minister, Northern Territory Treasury and the Central Holding Authority.

The preliminary results show that the Northern Territory's expenditure related to the Indigenous population (48.9 per cent) is greater than its revenue share (44.8 per cent).

An alternative analysis has been carried out to verify this result in the context of the Commission's Indigenous influences attribution. For general government agencies, excluding central agencies, if the Indigenous influences attribution is deducted from both the total expenditure and that related to the Indigenous population, the share of remaining expenditure related to the Indigenous population exceeds that of a per capita distribution. On this basis, Territory expenditure related to the Indigenous population is \$642 million, \$30 million more than the \$612 million implied by the Commission's Indigenous influences attribution and the impact of specific purpose payments.

### GST Revenue Projections

The Territory is heavily reliant on GST revenue funding from the Australian Government to meet its budgetary and fiscal needs. The Territory is susceptible to even slight variances in GST revenue, which can have a substantial impact on the Territory's fiscal position.

Accurate forecasting of the parameters that determine GST revenue can limit the risk to the Territory's budget. However, the lack of historical data on the GST, and the inherent difficulties in estimating the Territory's population and the Commission's relativities over the forward estimates period, make this process difficult.

The Territory's GST revenue grant is determined principally by:

- the total level of GST collected nationally;
- the Territory's share of the national population; and
- the Territory's per capita revenue-sharing relativity as determined by the Commission.

Unexpected changes in GST revenue parameters have a potential to pose risks (both upside and downside) to the Territory's financial position. In recent years there have been a number of examples where such risks have materialised.

These include:

- the Australian Government revising its 2002-03 national GST revenue estimate upwards by \$1.3 billion in its 2003-04 Budget due to the unexpected strength in the housing sector;
- the Territory experiencing negative population growth in 2002-03, following a period of above national average population growth; and
- a 1.5 per cent increase in the Territory's relativity in 2006-07, primarily due to data revisions, when a reduction was anticipated.

**GST Collections** In accordance with the Intergovernmental Agreement, the pool of national GST collections is made available to states. Variations in the size of the GST pool have a direct impact on the size of the Territory's GST revenue grant.

The Australian Government provides states with estimates of GST collections in its annual budget and in its Mid-Year Economic and Fiscal Outlook (MYEFO). Since the introduction of the tax in 2000, collections have been highly volatile and difficult to predict. The Australian Treasury remains the most informed source of GST estimates, given its access to the latest key statistical and collections data. On this basis, the Territory (and the states) have adopted the Australian Government estimate of the total GST pool over the budget and forward estimates period, however it should be cautioned that the underlying economic parameters used to calculate the Territory's GST revenue are estimates from the MYEFO which are six months old.

In its MYEFO, the Australian Government revised its 2005-06 GST estimate downward by \$627 million to \$36.7 billion. This was due to the overpayment of \$287 million of GST revenue in 2004-05 and the flow-on effect of this reduction to consumption in 2005-06. Reduced activity in the housing sector due to subdued house prices in most states made consumers cautious, resulting in reduced levels of consumption expenditure in 2004-05 and 2005-06.

The Australian Government has estimated GST growth of 6.8 per cent in 2006-07 reflecting a rebound in consumption off a reduced base (the 2005-06 base reflects the deduction of the 2004-05 overpayment), despite continuation of a subdued housing sector. According to the March 2006 Access Economics forecast, consumption may be further stimulated by Australian Government tax cuts and the impact of ongoing business investment. GST revenue growth from 2007-08 is expected to gradually return to its longer term assumed growth rate of 5.2 per cent.

**Territory's Share of the National Population** The Territory's share of national population is a second factor in determining its share of GST revenue. Variations in the Territory's population growth relative to the other jurisdictions have a direct impact on the Territory's GST revenue grant. The 2005-06 population estimates will be finalised in June 2006, when the Australian Statistician makes his final determination of the 2005-06 GST grant year population (as at 31 December 2005).

The Territory estimates its 2005-06 population growth at 1.7 per cent, significantly higher than the national growth rate of 1.2 per cent. This is a significant upward revision from the 2005-06 Budget forecast and is primarily due to positive interstate migration.

Territory population growth forecasts used in 2006-07 and ongoing from 2007-08 are 1.5 per cent and 1.2 per cent respectively. Territory population estimates are more conservative than Australian Government estimates, which forecast Territory population growth at 1.8 per cent in 2005-06, 1.6 per cent in 2006-07 and 1.3 per cent in forward years.

**Commonwealth Grants Commission's Relativities** The third element in determining the Territory's share of GST revenue is the recommendations of the Commission. The Territory's relativity has historically been the most volatile compared with the other jurisdictions. A small variation in the Territory's relativity has a significant impact on its GST revenue grant, posing a significant risk to the Territory's budgetary position. Neither the Australian Government nor the Commission provide estimates of future relativities.



In its 2006-07 Update, the Commission has assessed a relativity of 4.32755 for the Territory. Future relativities remain a considerable source of uncertainty. The Territory has forecast a moderate decline in relativity from 2007-08 onwards to account for anticipated revisions to the Commission's assessment of states' revenue capacity due to relative changes with other states in the property and mining sectors.

Table 5.4 shows the budget and forward projections for the Territory's GST revenue and the sensitivity of GST revenue to variation in key parameters. This analysis demonstrates that a change in any one GST parameter (in any particular year) can have a significant impact on the Territory's GST revenue. These impacts multiply when more than one parameter varies or when a trend emerges in forward years.

Table 5.4: Northern Territory GST Revenue Projections

	2005-06	2006-07	2007-08	2008-09	2009-10
<b>Budget Estimates (\$M)</b>	<b>1 829.4</b>	<b>1 967.7</b>	<b>2 062.3</b>	<b>2 125.8</b>	<b>2 196.6</b>
National GST Revenue (\$B)	36.7	39.2	41.3	43.5	45.8
Growth (%)	3.9	6.8	5.4	5.2	5.2
Population	204 258	207 322	209 810	212 328	214 876
Growth (%)	1.7	1.5	1.2	1.2	1.2
Share of National Population (%)	0.9985	1.0014	1.0015	1.0018	1.0023
Relativity	4.3	4.3	4.3	4.2	4.2
<b>Sensitivity to a one percentage point variation in growth in key parameters</b>					
National GST Revenue					
One year only variation (\$M)		15.9	16.9	17.5	18.2
Ongoing variation (\$M)		15.9	33.7	52.8	73.5
Population					
One year only variation (\$M)		19.4	20.4	21.1	21.8
Ongoing variation (\$M)		19.4	41.0	63.7	88.1
Relativity					
One year only variation (\$M)	na	na	21.6	22.3	23.0
Ongoing variation (\$M)	na	na	21.6	44.5	69.0

## National Competition Payments and National Reform Agenda

Competition payments were introduced in 1997 in accordance with National Competition Policy (NCP) arrangements agreed by the Council of Australian Governments (CoAG) in 1995. The NCP agreements require governments to review all legislation that restricts competition, ensure competitive neutrality in the operations of government businesses, reform public monopolies and comply with national reform frameworks relating to energy, water and road transport sectors.

In recognition that the benefits of NCP accrue disproportionately to the Australian Government through its income tax base, financial assistance payments are provided to the states and territories to ensure an equitable distribution of the dividends of national reform. Payments are subject to compliance with NCP reform commitments, as assessed by the National Competition Council (NCC).

The Territory's 2005-06 competition payment entitlement is around \$8 million. The NCC's 2005 assessment recommended a permanent deduction of 5 per cent (\$0.4 million) of 2005-06 payments for the Territory for the retention of restrictions on takeaway liquor trading. However, this recommendation was not accepted by the Australian Government in recognition of the considerable work being undertaken by the Territory in mitigating alcohol-related harm.

Actual 2005-06 competition payments are now contingent upon the outcomes of the final assessment of NCP water reform by the National Water Commission, expected by mid 2006. The current NCP program, including competition payments, expires after 2005-06.

On 10 February 2006, CoAG agreed to a new national reform framework to maintain national economic performance and living standards into the future. The new framework is known as the National Reform Agenda (NRA) and is more broadly based than NCP and comprises three broad streams in human capital, competition and best practice regulation.

The NRA reforms are to be implemented through agreed intergovernmental action plans which will detail agreed reform actions, progress measures and outcomes.

Under the NRA, the Australian Government is to consider financial assistance to the states and territories on a case by case basis, with reference to the distribution of costs and benefits between levels of government. The quantum and timing of financial assistance will be determined as part of the development of NRA intergovernmental plans during 2006.

A new statutory authority, the CoAG Reform Council (CRC), is to be established to monitor and assess reform progress against intergovernmental plans and report annually to CoAG. The CRC will subsume the current role of the NCC. The Australian Government will determine eligibility for financial assistance based on CRC reports. At this stage, no revenue for this source has been factored into the Budget from 2006-07.

## Other Australian Government Grants

The majority of other Australian Government grants are classified as specific purpose payments (SPPs), which are usually tied to some specific program or function against which they must be acquitted. SPPs are a major mechanism by which the vertical fiscal imbalance between the Australian and state levels of government is corrected.

In 2006-07, the Territory will receive about \$446 million in other Australian Government grants, representing 15 per cent of total general government revenue.

SPPs are usually governed by formal agreements between the Australian Government and the states which set out conditions such as:

- the programs and functions for which the funds may be used;
- the contribution of state discretionary funds;
- restrictions on how funded programs may be delivered;
- performance and reporting requirements; and
- punitive sanctions for the breach of other conditions in the agreements.



## General Issues with SPPs

Although SPPs are a means of reducing vertical fiscal imbalance between the states, they also provide the Australian Government with the ability to exert a policy influence over areas of service provision which are historically or constitutionally a state responsibility. SPPs are increasingly regarded by the Australian Government as a means of aligning the delivery of state services with its own policy objectives.

SPPs are an accepted feature of Australian intergovernmental financial relations, and are an important source of revenue for the states. Nonetheless, there are numerous problems with the current implementation of SPP arrangements, including:

- inefficiency – SPPs carry a large administrative burden and involve duplication of functions at the national and state levels of government;
- distortion of services – the input controls and performance requirements in SPPs often do not promote optimal outcomes, and stifle innovation in service delivery; and
- reduced budget flexibility – input controls in SPP agreements effectively control large amounts of state discretionary revenue, substantially reducing state budget flexibility.

## The Way Forward

The states have approached the Australian Government repeatedly in recent years to seek agreement on a set of principles and guidelines for the negotiation of future SPP agreements. These may include:

- the simplification of reporting requirements;
- the use of output performance measures in preference to input controls; and
- greater flexibility in the use of SPP funding.

The indications are that the Australian Government is not prepared to consider SPP reform at present. The Australian Government has generally hardened its position, using SPP agreements to promote its industrial relations agenda, introducing stronger input controls, and applying financial penalties for technical breaches of SPP agreements, such as missing reporting deadlines.

## Major Agreements Negotiated in 2005-06

### Skilling Australia's Workforce (SAW)

The new SAW agreement, covering funding from 2005-08, replaces the former Australian National Training Agreement (ANTA). The SAW agreement, which was finalised in early 2006, marks a significant change in funding and governance arrangements for the vocational education and training (VET) sector. The Australian Government is expected to provide \$60.2 million over the term of the agreement to the Territory. The Northern Territory's funding commitment over the same period is \$243.9 million.

The new SAW agreement contains a significant number of performance targets for the Territory. These include:

- enhancing competition through user choice;
- increasing training numbers in identified skills shortage areas;
- creating additional training places for mature age people, youth and disabled people; and
- increasing participation by Indigenous Territorians at higher qualification levels.

### Supported Accommodation Assistance Program V (SAAP V)

The national SAW agreement is supported by a bilateral agreement between the Australian and Northern Territory governments and the 2006-08 VET Plan, which sets the direction and identifies priorities for VET in the Territory.

SAAP V is a five-year agreement commencing in 2005-06. The agreement provides funding to transitional supported accommodation and other support services to help people who are homeless or at imminent risk of becoming homeless. The aim of the program is to help these people achieve the maximum possible degree of self-reliance and independence. The Australian Government is expected to contribute \$25.5 million over the term of the agreement, with the Northern Territory Government required to contribute a minimum of \$21.9 million.

Under the arrangements in the SAAP V agreement, the Northern Territory Government is responsible for the routine administration and management of the program, with the Australian Government assuming responsibility for national aspects such as the development of a national strategic plan, evaluation, research and reporting.

During negotiations over the SAAP V agreement, the states sought an increase in Australian Government SAAP funding commensurate with demand and cost pressures on SAAP services. However Australian Government funding was largely unchanged, with a significant portion diverted from SAAP services into an Innovation and Investment fund controlled by the Australian Minister for Family and Community Services. A significant increase in Northern Territory funding was therefore required just to maintain existing SAAP services.

Australian Government funding for SAAP V related activities is expected to be 8 per cent higher in 2009-10 than in 2005-06; however over the same period, Northern Territory Government funding is set to increase by more than 50 per cent.

### Indigenous Housing and Infrastructure Agreement (IHIA)

In 2005 a new agreement on Indigenous housing and related infrastructure was signed between the Australian and Northern Territory governments. The two year agreement is effective from 1 July 2006. The Australian Government has committed to provide up to \$64.3 million in 2006-07.

The purpose of the agreement is to amalgamate and streamline existing bilateral funding and governance agreements for Indigenous housing and housing-related infrastructure services, including the:

- Northern Territory component of the Community Housing and Infrastructure Program (\$17.3 million in 2006-07);
- Northern Territory Indigenous housing component of the National Aboriginal Health Strategy (\$22.0 million in 2006-07);
- Healthy Indigenous Housing Initiative Program (\$4.7 million in 2006-07); and
- Housing Assistance for Indigenous People component of the Commonwealth-State Housing Agreement (\$20.2 million in 2006-07).

The Northern Territory Government is the primary manager and deliverer of Indigenous housing and related services in the Territory. IHANT plays a key advisory role, while the Australian Government continues to take responsibility for provision of municipal infrastructure and municipal and essential services to Indigenous outstations and homelands.



The new arrangements will result in the Northern Territory Government receiving a significantly higher level of total funding for Indigenous housing. This higher amount reflects the pooling of funding from various Australian Government sources. The Australian Government has committed that the Territory will not be worse off should the additional payments result in a change to relativities as assessed by the Commonwealth Grants Commission.

**Royal Darwin Hospital  
– Trauma Centre**

In 2005, a five-year agreement was signed to establish the Royal Darwin Hospital (RDH) as the National Critical Care and Trauma Response Centre. Under the agreement, the RDH will assist in the development of Australia's frontline preparedness and emergency response capability, due to its strategic position in relation to Australia's defence and international activities in the Asia-Pacific region.

Australian Government funding for this agreement totals \$61.4 million, of which \$21 million was provided in 2005-06, with \$13.2 million estimated to be provided in 2006-07.

