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Sovereign States and National Power: Transition in Federal - State Finance

by

John Wilkinson

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EXECUTIVE SUMMARY

- Originally the federation, of the former British colonies on the continent of Australia, was based on the assumption both that the newly formed states would be financially stronger than the central government and that the major share of decisions on important matters would remain with state administrations (pp.2,8)

- Certain key areas of decision-making, conducive to the consolidation of the states into a nation, were allocated to the newly established federal government (p.2)

- From the inauguration of federation onwards, the federal government sought to direct to itself the greater part of revenue raised in the country (pp.8,11)

- It was the Australian Labor Party that first sought to extend the control of the national government into significant realms of decision making – principally for social objectives (pp.3-8). The Australian Labor Party was also initially inclined to utilise tariffs to stimulate the establishment and expansion of production in Australia (pp.4,15). The ALP was particularly concerned with not only drawing financial control towards the central government, but in having the central government direct expenditure (pp.13-14)

- Since the beginning of federation, there have always been disparities between the states as far as their respective capacities to raise revenue are concerned (pp.10,38)

- To address the differences in revenue raising capacities, amongst the states, the federal government established a Commonwealth Grants Commission (pp.10-11,21-23)

- After the federal government gained control over the levying of income tax, the states and territories have become increasingly dependent on revenue from the federal government (pp.11-14,20-34)

- During the 1980s and 1990s the Australian Labor Party not only forsook the policy of government control over production and commerce (favouring policy based on markets), but actively embarked on facilitating the functioning of state-based enterprises on a national level. The Howard Government has pursued similar policies (pp.14-20)

- Currently the Commonwealth Grants Commission continues to determine the shares in the newly established system of federal funding – prompting remonstrations from states which consider they are dealt with unfairly (pp.26-39)

1.INTRODUCTION

In April 2005 the prime minister, John Howard, delivered a speech in which he reflected on the past nature of the states in Australia, in contrast to the federal government, and on what form the relationship might take in the future. In particular he said that,

> I'm here. . .to make some remarks on Australian federalism. . .We know that if Australia is to grow and prosper in the 21^{st} century we must embrace continuous reform. . .I believe that part of that change is a greater focus by the Australian people on ties to nation and to local community, and less on traditional state loyalties. . .When I was a young solicitor in Sydney in the early 1960s, our legal firms were confined exclusively to state capitals. . .Today, of course, that is no longer the case. . .In the vital area of education, the increased mobility of our population means that no fewer than 80,000 Australian students move from one state or territory to another each year. . .A single set of national laws on industrial relations is [also] an idea whose time has come. . .[1]

This paper looks at the changes that have taken place in Australian federalism: particularly changes in financial relations between the national government and the states and territories. It examines the early period in the federation, when the financial resources of the central government were relatively less substantial compared to the states, and proceeds to look at how the central government achieved financial predominance and the situation of the states in the present era.

2.INITIAL TRANSITION FROM INDIVIDUAL COLONIES TO NATION

(a)Origins of the States as Individual British Colonies

Australia does not operate like a unitary state (unlike Britain) because, between the arrival of British people in Australia and the beginning of the twentieth century, there was no Australian nation on the continent of Australia. What was established, on the continent of Australia, were a number of individual British colonies. If a British citizen left England for Australia, they did not come to Australia. They came to New South Wales or Victoria, or to one of the other independent British colonies on the Australian continent. There they became a resident within that colony.[2]

It is not surprising therefore that, as the spread of commerce induced the leaders of those colonies to consider a closer association, those same leaders approached such a development on the basis of retaining as much of their pre-existing status as possible. As

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1 John Howard, Prime Minister of Australia, *Reflections on Australian Federalism*. Speech delivered at the Menzies Research Centre, Melbourne, April 2005.

2 W.J. Campbell wrote that, each British colony established in Australia, after 1788, was "a unit of self-government within the British Empire. . .owing separate allegiance to the Imperial Crown." See W.J. Campbell, *Australian State Public Finance* (Law Book Company of Australia, Sydney, 1954), p.11.

Gordon Greenwood later described these developments, "The aim of those who set up [what would be] the Commonwealth was to allow the [future] states to maintain their power to the full, except upon a limited number of enumerated subjects".[3] Although, to underwrite the viability of the new entity, each of the former independent colonies transferred their greatest source of revenue (customs and excise) to the Commonwealth, the states, however, retained their right to levy land tax and income tax, and the right to impose stamp duties.[4]

(b)Beginning the Transformation towards a Nation

Although what was brought into existence in 1901 was, in many ways, a confederation of states, the combined effects of threats from outside – as well as the expansion of commerce and the desire for social equality within - began to stimulate the formation of a nation. Indeed those very "enumerated subjects" entrusted to the Commonwealth were in fact exactly those powers conducive to the production of a nation from a collection of states. As Greenwood also observed,

> The principal powers entrusted to the Commonwealth [on the inauguration of federation in 1901] consisted of the. . .right to legislate with respect to defence, external affairs. . .immigration, posts and telegraph, banking and currency, foreign and inter-state trade, and commerce and industrial arbitration in cases where the dispute extended beyond the limits of one state.[5]

Even more relevant was the fact that, in the conferences that led to the formation of federation, some colonial leaders were already highlighting the national implications of the venture. John Macrossan (appointed colonial secretary in Queensland in 1890) declared at the National Australasian Convention, held in Sydney the following year, that he hoped what was about to come into being would consist of "first Australians and then Queenslanders and South Australians and Victorians".[6] Edmund Barton, the first prime minister of the newly established Commonwealth of Australia, declared that what had now come into existence was "a continent for a nation, and a nation for a continent".[7]

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3 Gordon Greenwood, *The Future of Australian Federalism: A Commentary on the Working of the Constitution*, second edition (University of Queensland Press, Brisbane, 1976), p.57. As Julie Smith expressed it, New South Wales and Victoria "expected to exercise. . .control" over the new entity. See Julie Smith, *Taxing Popularity: The Story of Taxation in Australia* (Federalism Research Centre, Australian National University, Canberra, 1993), p.41.

4 Greenwood, op.cit., pp.79-80. See also Campbell, op.cit., pp.64-71.

5 Greenwood, op.cit., pp.58,117.

6 Harrison Bryan, "John Murtagh Macrossan" in Margaret Cribb, Roger Joyce and Denis Murphy (eds.), *The Premiers of Queensland*, revised edition (University of Queensland Press, Brisbane, 1990), p.111.

7 W.K. Hancock, "The Commonwealth, 1900-1914" in Ernest Scott (ed.), *The Cambridge History of the British Empire*, vol.VII, part 1, *Australia* (Cambridge University Press, Cambridge, 1933), p.491.

3.THE ALP AND COMMONWEALTH POWER FOR SOCIAL OBJECTIVES

(a)The Australian Labor Party and the Accumulation of Commonwealth Power

During the nineteenth century, the reach of government (in the British colonies in Australia) had been extended into areas which, in Britain itself, had been preserved for business. Thus in 1855 the NSW colonial government had taken over the running of the railways (mainly, however, because of the incapacity of local business people to finance such an operation).[8]

During the early years of the twentieth century, aspirations for social progress led the political representatives of the recently formed Australian Labor Party to extend the reach of the (Commonwealth) government to provide the means to introduce legislation both for the control of industry and for increased social welfare. As L.F. Crisp remarked, in those states where the ALP representatives in the lower houses were in a majority, the party had introduced policy for social welfare only to find it blocked by "property-franchised state legislative councils."[9] The ALP then decided that, if it gained power at a federal level, it would obtain the passage of legislation that would apply to everyone in Australia, regardless of the legislative councils. ALP politicians in turn, even when Labor did gain power nationally, found the aims of the party thwarted by the constitution. Harrison Moore wrote that,

> when a Labour government assumed office in 1910, it introduced a set of alterations extending the Commonwealth power to all trade and commerce, combinations and monopolies in relation to the production, manufacture or supply of goods or services, the control and regulation of corporations, and labour and employment. . . The proposals were passed without difficulty through both houses of parliament, but on the referendum held in accordance with the constitution, they were rejected by the voters by an overwhelming majority. . .[10]

Although the ALP's aspirations had been denied by the referendum, it remained determined to introduce government control into production and commerce. In New South Wales the McGowen government acted on this principle, in the realm of rural irrigation, when it obtained the passage of *Water Act 1912* and the *Irrigation Act 1912*: both pieces of legislation not only preserving the earlier *Water Rights Act 1896* (which vested ownership of water in the state) but providing for the establishment of a Water Conservation and Irrigation Commission (WCIC) which would supervise the building of dams and the issuing of water licences.[11] The long-term rationale behind the WCIC was that irrigated

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8 Robert Lee, *The Greatest Public Work: The New South Wales Railways 1848-1899* (Hale and Iremonger, Sydney, 1988), pp.15-23.

9 L.F. Crisp, *Australian National Government*, fourth edition (Longman Cheshire, Melbourne, 1978), p.185.

10 W. Harrison Moore, "The Constitution and its Working" in Scott, op.cit., p.477.

11 Water Conservation and Irrigation Commission, *Water Resources of New South Wales* (NSW Water Conservation and Irrigation Commission, Sydney, 1971), pp.133-135; Trevor Langford-Smith, "Murrumbidgee Irrigation Development: A Study of Irrigation Planning,

areas of the state would produce commodities which would then be exported to Britain on the basis of protected trading arrangements with the latter. As C.J. King outlined, "In 1924 imperial tariff preferences granted certain concessions with respect to canned fruits and dried fruits."[12]

The crisis of the First World War gave the ALP an opportunity to introduce government into production and commerce at least on a temporary basis. In 1915 Andrew Fisher's ALP government, as D.B. Copland described, "entered in an arrangement with the governments of New South Wales, Victoria, South Australia and Western Australia, under which. . .an Australian Wheat Board [AWB] was set up. . .the Wheat Board purchased the wheat from farmers. . .The scheme was continued for the remaining harvests during the war, and for two years after."[13]

As well as trying to reintroduce its aims of controlling production and trade via temporary wartime measures, the ALP began to argue for the abolition of state governments. In 1917 a conference of the Victorian section of the Australian Labor Party approved a motion which called for the elimination of state parliaments. A year later, this was made part of the ALP's federal policy: calling for "Unlimited legislative powers in Australian affairs to be vested in the Commonwealth parliament". As L.F. Crisp remarked, "One of the Labour motives for seeking unification was, of course, to get existing state legislative powers away from the dead hands of. . .property-franchised state legislative councils." But, as Crisp further observed, "above all, Labour insisted that it wanted national problems and national aspirations tackled upon a national basis for the benefit of the whole nation."[14]

Meanwhile even non-ALP governments began extending government into production. In Victoria, in 1921, the Nationalist Party state government in Victoria (then led by Harry Lawson) established the State Electricity Commission: headed by the distinguished soldier John Monash. Indeed, as Malcolm Abbott has written,

> After World War I, developments in high voltage transmission provided opportunities for the development of [publicly owned] enterprises. From the 1920s

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Establishment and Growth" in Trevor Langford-Smith and John Rutherford, *Water and Land: Two Cases in Irrigation* (Australian National University Press, Canberra, 1966), p.28.

12 C.J. King, *An Outline of Closer Settlement in New South Wales*, part 1, *The Sequence of the Land Laws 1788-1956* (NSW Department of Agriculture, Sydney, 1957), p.238. In the 1880s, Britain had taken 75% of Australia's exports. During the 1930s, Britain still obtained, from Australia, 31% of its wheat imports; 15% of its butter imports; 12% of its apple and pear imports; and 10% of its sugar imports. Britain also took (annually) nearly all Australia's exports of beef. See Brian Pinkstone, *Global Connections: A History of Exports and the Australian Economy* (Australian Government Publishing Service, Canberra, 1992), p.88; Charles Smith, *Britain's Food Supplies in Peace and War* (Routledge, London, 1940), pp.25,49; R. Duncan, "Imperial Preference: The Case of Australian Beef in the 1930s" in the *Economic Record*, vol.39, no.86, June 1963, p.159; Nancy Windett, *Australia as Producer and Trader* (Oxford University Press, London, 1933), pp.109,118.

13 D.B. Copland, "Australia in the World War: Economic" in Scott, op.cit., pp.594-495.

14 Crisp, op.cit., p.185.

> . . . state authorities were developed in each state. . .In four states – Victoria, South Australia, Western Australia and Tasmania – a central authority gradually achieved control over the greater part of generation, transmission and distribution.[15]

In 1930, in the depths of the trade depression, the ALP prime minister (Scullin) introduced a bill into the federal parliament – the *Constitution Alteration (Power of Amendment) Bill* – which would have given the federal parliament full power over amending the constitution. This stratagem failed, however, because the ALP did not have a majority in the Senate.[16]

(b)The ALP and the Extension of National Power: 1940s-1970s

Eleven years after Scullin's failed attempt at consolidating further power in the hands of the Commonwealth government, and just two years after the war in Europe had been in progress, the ALP were able to form a federal government. John Curtin, who led the government, held many of the ALP's sentiments on the advantages of national power. As David Day has written, whereas under Menzies (the previous prime minister) "Melbourne had been the de facto capital, with most meetings of the war cabinet being held there rather than in Canberra", Curtin announced that Canberra was "the seat of Australia's government, and his government would operate from Canberra".[17]

In 1943 the ALP (still led by Curtin) gained a majority in both the House of Representatives and the Senate. On the basis of this, the ALP tried once more to further consolidate power in the hands of the national government. A year later, Curtin obtained passage of the Postwar Reconstruction and Democratic Rights Act: providing for a referendum to be held which would allow the Commonwealth government, for a period of five years after the end of the war, to make laws in fourteen areas of concern including employment, trusts, profiteering and production and distribution of goods. The public, however, voted in the majority against the referendum proposals.[18]

Despite this setback, after the war the ALP federal government (led by Chifley after Curtin's death in 1945) continued to consolidate national power in the hands of the Commonwealth (until its defeat in the general election of 1949). In 1945 the Chifley government obtained passage of a new *Commonwealth Bank Act* replacing previous legislation since the bank was first established in 1912. This new legislation formally elevated the already existing Commonwealth Bank into Australia's central bank (the central banking powers being later transferred by Menzies to a new Reserve Bank in 1959). It also provided the bank with trading as well as savings operations. A key provision of the

15 Malcolm Abbott, "The Performance of an Electricity Utility: The Case of the State Electricity Commission of Victoria 1925-93" in the *Australian Journal of Economic History*, vol.46, no.1, March 2006, p.26.

16 Brian Galligan, *No Bill of Rights for Australia* (Australian Senate, Canberra, 1989).

17 David Day, *John Curtin: A Life* (Harper Perennial, Sydney, 2006), p.523.

18 Kylie Tennant, *Evatt: Politics and Justice* (Angus and Robertson, Sydney, 1970), pp.159-162.

legislation was the requirement that the commercial banks lodge a substantial proportion of the funds in "special accounts" with the Commonwealth Bank. This was to enable the Commonwealth Bank to restrict the commercial banks' lending during booms and loosen control on that lending during busts. Section 48 of the *Commonwealth Bank Act 1945* also stipulated that "Except with consent in writing of the Treasurer, a bank shall not conduct any banking business for a state, or for any authority of a state, including a local government authority." Melbourne City Council, which had banked with the National Bank of Australasia (the present-day NAB) appealed to the High Court which, in turn (in 1947), held section 48 to be invalid. Chifley then obtained passage of the *Banking Act 1947*: providing for the nationalisation of banking in Australia (by having the Commonwealth Bank take over the commercial banks). The commercial banks appealed to the High Court and, a year later, the court found the legislation invalid. The original *Commonwealth Bank Act 1945*, however, remained.[19]

Meanwhile, in the same year that the ALP obtained passage of the original *Commonwealth Bank Act*, the Chifley government obtained passage of the *Pharmaceutical Benefits Act 1945* which would have made all drugs, on a Commonwealth Schedule, free of charge. This was soon challenged by the British Medical Association (the then representative body of Australian doctors) in the High Court: the latter finding the legislation unconstitutional. Similarly in 1945, Chifley obtained passage of the *Australian National Airlines Act*: providing for the nationalisation of inter-state air services in Australia (subsequently the High Court reduced the scope of the legislation, allowing only for the federal government to operate an airline in competition with other commercial airlines: this body becoming known as Australian Airlines).[20] A year after he obtained passage of the *Australian National Airlines Act*, Chifley secured passage of legislation providing for the Australian government's purchase of the stake held by the British Overseas Airways Corporation (BOAC) in (the then) Qantas Empire Airways (QEA). Another year later, in July 1947, Chifley effected government ownership of (what would become) QANTAS when it purchased all 261,500 of QEA's shares.[21]

In 1946 the Chifley government presented a referendum to the people requesting that they approve the transfer of social services provision from the states to the federal government. This was approved in the majority.[22] In the same year that this referendum was approved,

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19 Boris Schedvin, *In Reserve: Central Banking in Australia 1945-75* (Allen and Unwin, Sydney, 1992), pp.68,70,83,86. In his second reading speech, for what would become the *Banking Act 1947*, Chifley declared that "the Labour Party has held further that, since private banks are conducted primarily for profit and therefore follow policies which in important respects run counter to the public interest, their business should be transferred to public ownership." See A.W. Stargardt (ed.), *Things Worth Fighting For: Speeches by Joseph Benedict Chifley* (Melbourne University Press, Melbourne, 1952), p.105.

20 Judith Healy and Melinda Hilless, *Health Care Systems in Transition: Australia* (European Observatory on Health Care Systems, Copenhagen, 2001), p.13; Stargardt, op.cit., p.89.

21 John Gunn, *Challenging Horizons: QANTAS 1939-1954* (University of Queensland Press, Brisbane, 1987), pp.184,196,203,207-208,214-221,236-237,257,261.

22 Tennant, op.cit., p.206.

Chifley obtained passage of the *Hospital Benefits Act 1946* under which, as Judith Healy and Melinda Hilless have described, "the Commonwealth entered into agreements with the states to subsidise hospital beds on the condition that there was no charge for patients in public wards. . .This has remained the basis of subsequent hospital financing agreements between the Commonwealth and the states."[23]

Two years later, Chifley extended the control of the federal government into the trading of commodities when he secured passage of the *Wheat Industry Stabilisation Act 1948* which established the present-day Australian Wheat Board: the purpose of which was to allow small-scale wheat growers to bypass the big commercial grain trading companies (which they felt had bargained them down) and sell their wheat to a sole (government-owned) buyer which would uphold the price.[24]

A year after gaining passage of legislation establishing the Australian Wheat Board, Chifley obtained passage of the *Snowy Mountains Hydro-Electric Power Act 1949*. As Lionel Wigmore outlined, "The Act. . .decreed that there should be established a Snowy Mountains Hydro-Electric Authority empowered to 'construct, maintain, operate, protect, manage and control' works for "the collection, diversion and storage of water in the Snowy Mountains area', and for generating and transmitting electricity."[25] The scheme took twenty-five years to complete.

In the same year that the Snowy Mountains Scheme was launched, the ALP government in New South Wales (led by James McGirr) announced that it would place the generation of electricity in the state in the hands of a single authority and, in May 1950, the Electricity Commission of New South Wales (ECNSW) was established.[26] Again, as in the case of government ownership of the NSW railways (nearly a century before) this move was to help business as much as any other segment of society. The chair of the Colliery Proprietors' Association (Sir Edward Warren) declared, a year after the 1965 election of a Liberal Party-Country Party government in the state, that "in many respects the previous [ALP state governments] did a good job. I cite as an example of this good work the establishment of an efficient electricity generation and supply industry."[27]

Although Curtin had continued a fundamental shift of power from the states to the federal government, a substantial degree of control still remained with the states. Robert Menzies' Liberal Party-Country Party government, which gained power in the 1949 election, reduced

23 Healy and Hilless, op.cit., p.14.

24 Greg Whitwell and Diane Sydenham, *A Shared Harvest: The Australian Wheat Industry 1939-1989* (Melbourne University Press, Melbourne, 1991), pp.43,59-60.

25 Lionel Wigmore, *Struggle for the Snowy: The Background of the Snowy Mountains Scheme* (Oxford University Press, Melbourne, 1968), p.148.

26 C.R. Hall, *The Manufacturers: Australian Manufacturing Achievements to 1960* (Angus and Robertson, Sydney, 1971), pp.741-743.

27 George Wilkenfeld, *The Electrification of the Sydney Energy System 1881-1986* (PhD Thesis, Macquarie University, 1989), p.211.

the drive for Commonwealth power: leading to the ALP still regarding the states' power as an impediment to the achievement of social objectives. In the late 1950s a newly elected member of the House of Representatives, Edward Gough Whitlam, declared that, because of the continuing division of power between the federal government and the states, the ALP still found "it useless to promise its basic policies." It was handicapped, Whitlam maintained, "by a constitution framed in such a way as to make it difficult to carry out Labor objectives and interpreted in such a way as to make it impossible to carry them out."[28]

On winning the 1972 election, as the leader of an ALP government, Whitlam re-embarked on extending national power for social objectives. After the subsequent 1974 election, Whitlam obtained passage of legislation establishing a national health insurance scheme (Medibank) under which doctors could directly bill the newly established Health Insurance Commission (HIC) for their patients ("bulk billing"), or patients could claim back, from the HIC, 85% of a (scheduled) fee for a medical service.[29] The Whitlam government also took over full responsibility for financing students' attendance at university.[30]

4.SHIFT IN FINANCIAL CONTROL FROM THE STATES TO THE COMMONWEALTH

(a)Contests over Federal-State Finance

Although the states had considered that they had, both individually and collectively, much greater productive strength than the Commonwealth, the latter began to demonstrate its financial potential almost as soon as the federation came into existence. As stated above, the former independent British colonies had agreed that, on the commencement of federation, their customs and excise levies (hitherto their main source of revenue) would be handed over to the Commonwealth. Although (on the insistence of the Tasmanian premier Sir Edward Braddon) the colonial premiers had adopted the provision that - for the first ten years of federation - 75% of the customs and excise revenue raised by the Commonwealth would go back to the new states, the colonial premiers had also agreed that after the ten years had elapsed the new federal government could keep all its customs and excise revenue. In 1910, just as the states were about to lose their 75%, the newly elected ALP government (led by Andrew Fisher) obtained passage of the *Surplus Revenue Act* which provided that, out of the customs and excise revenue (which the federal government would now retain) the Commonwealth would give to each state a grant amounting to 25 shillings for each person resident in the state.[31]

28 Galligan, *No Bill of Rights for Australia*.

29 Healy and Hilless, op.cit., p.15.

30 Russell Mathews and Bhajan Grewal, *Fiscal Federalism in Australia: from Keating to Whitlam* (Centre for Strategic Economic Studies, Victoria University, Melbourne, 1995), p.9.

31 Hancock, op.cit., in Scott (ed.), p.498.

During the First World War, however, the Commonwealth government (led at the beginning of hostilities by Cook) found itself with an ever-increasing financial burden. Apart from borrowing, federal expenditure on the war, from revenue, rose from £640,218 in financial year 1914-1915 to £21.2 million in 1918-1919. To increase its revenue raising capacity, Cook (prime minister until 1914), Fisher (prime minister from 1914-1915) and then Hughes (prime minister from 1915 onwards) oversaw the introduction of new forms of direct tax: the most important of which was income tax. By financial year 1917-1918, income tax amounted to 30% of federal revenue, as the following table indicates:

Federal Tax Collected: 1917-1918[32]

Customs and Revenue	£13,200,000
Income Tax	£7,400,000
Other Taxes (Including Land and Entertainment Tax)	£4,000,000
TOTAL	£24,600,000

During the 1920s the federal government decided to keep its newly acquired income tax powers, despite the development of a situation where both the federal government as well as the states now levied income tax and where the latter remained an important source of revenue for the states. Meanwhile national governments had also become frustrated with having to maintain the 25 shillings per person payments to the states. In 1926 the Nationalist Party-Country Party federal government (led by Stanley Bruce and Earle Page) indicated that it would try wind up this arrangement via passage of legislation. This move was resisted by New South Wales, and the other states, because even these so-called "population" grants (while now considerably less than the original 75% of customs and excise) still contributed significantly to state revenue. The relative importance of income tax, and the population grants, for New South Wales revenue can be seen in the following table for 1926-1927:

New South Wales Revenue 1926-1927[33]

Population Grant	£2.9 million (8%)
Income Tax	£7.7 million (21%)
Income from other Sources (incl. Business Undertakings)	£33.5 million
TOTAL	£44.1 million

Through the stratagem of the 1927 financial agreement between the Commonwealth government and the states – under which, as Schedvin has described, "all borrowing in Australia and abroad was in the name of the Commonwealth against the issue of Commonwealth government securities. . .[and] the Commonwealth accepted responsibility

32 Copland, op.cit., in Scott (ed.), p.592.

33 *Official Year Book of New South Wales 1926-1927* (New South Wales Government, Sydney, 1928), pp.388,402.

for existing debt”[34] - the Bruce-Page government swapped its commitment to pay population grants with a commitment to use the financial equivalent of a state’s population grants to supplement that state’s public debt repayment.[35]

(b)Disparities Between the States

By the 1920s it was becoming clear that some states had a greater capacity than others to produce tax revenue. In the mid-1920s, Professor Lyndhurst Giblin (chief statistician of Tasmania) prepared the following table of the federal income tax capacities of the states:

Federal Income Tax per Capita as a %age of National Average: 1921/22 to 1923/24[36]

Victoria	124%
South Australia	107%
New South Wales	98%
Western Australia	84%
Queensland	72%
Tasmania	62%

In 1932, during the depths of the 1930s depression, the Western Australian state government decided to hold a referendum on seceding from the federation (as a way of manifesting its frustration over financial arrangements with the Commonwealth). The prime minister at the time (Joseph Lyons of the United Australia Party, precursor of the Liberal Party) visited Western Australia to campaign for the no vote. To bolster the vote against secession, Lyons announced that he would establish a commission to examine the need for special grants to the states. The motion in favour of secession received a majority of votes but the same people in Western Australia, in a state election held later in the year, voted in a government that was against secession. Nevertheless the Lyons government went ahead and established a Commonwealth Grants Commission (CGC) which, from the 1930s to the 1970s, recommended to successive federal governments the extent of small, special grants which should be made to the financially weaker states of Western Australia, South Australia and Tasmania.[37]

34 Schedvin, op.cit., p.26. In financial year 1926-1927 the total amount of money raised from bondholders, by all the Australian states (from their inauguration as colonies onwards) currently amounted to £641 million. The three states with the biggest shares of this amount were New South Wales (£234 million), Victoria (£137 million) and Queensland (£102 million). See *Official Year Book of New South Wales 1927-1928* (New South Wales Government, Sydney, 1929), p.443.

35 Russell Mathews and Robert Jay, *Federal Finance: Intergovernmental Financial Relations in Australia since Federation* (Nelson, Melbourne, 1972), p.121.

36 Ross Williams, “Fiscal Federalism: Aims, Instruments and Outcomes”, paper delivered at the *Conference of Economists*, University of Melbourne, 27 September 2005, p.18.

37 Commonwealth Grants Commission, *Equality in Diversity: Fifty Years of the Commonwealth Grants Commission* (Australian Government Publishing Service, Canberra, 1983), pp.6-16; Peter Groenewegen, *Public Finance in Australia: Theory and Practice*, third edition (Prentice Hall, Sydney, 1990), p.255.

(c)War in the Pacific and the Shift in Federal Financial Power

During the period between Hitler's attack on Poland (1939), and Japan's invasion of the British, French and Dutch colonies in Asia (just after Curtin became prime minister), Australian federal spending on war preparations rose from £14 million to £562 million.[38] In April 1942, following the outbreak of the Pacific War and the threat of attack from Japan, John Curtin (prime minister of the then ALP federal government) held a conference with the state premiers. Curtin emphasised his intention that Australia's involvement in the war would be financed, as much as possible, by taxation. For this purpose he proposed that the federal government take over all income tax raising in Australia. According to James Maxwell, he informed the premiers "that if the states withdrew from income tax, the Commonwealth would guarantee the right of re-entry at the end of the war."[39] With the premiers refusing the offer, Curtin introduced four bills into the federal parliament providing for the transfer of income tax powers to the Commonwealth for the period of the war and one year afterwards. All the bills became Acts. The *Income Tax Act 1942* set an income tax rate higher that the combined existing Commonwealth and state rates; the *Income Tax Assessment Act 1942* gave priority to payment of the Commonwealth income tax over state income tax; the *Income Tax (War Time Arrangements) Act 1942* provided for the Commonwealth to take over state income tax staff, premises, facilities and records.[40] The last bill – which became the *States Grants (Income Tax Reimbursement) Act 1942* – offered the states a grant instead of the income tax that they would otherwise have raised.[41] Four states (Victoria, Queensland, South Australia and Western Australia) lodged appeals in the High Court against the legislation, but the court upheld its validity.[42] The first grant that New South Wales received, in financial year 1942-1943, was £11.3 million or around 16% of the state's total revenue as indicated by the table below:

New South Wales Revenue 1942-1943[43]

Tax Reimbursement Grant	£11.3 million
Income from other Sources (incl. Business Undertakings)	£60.2 million
TOTAL	£71.5 million

38 Crisp, op.cit., p.116.

39 James Maxwell, *Commonwealth-State Financial Relations in Australia* (Melbourne University Press, Melbourne, 1967), pp.48-50.

40 Rodney Fisher and Jacqueline McManus, *The Long and Winding Road: A History of Centralisation in Australian Tax* (Australian Taxation Studies Program, University of New South Wales, Sydney, 2002), p.8.

41 Mathews and Jay, op.cit., pp.174-175.

42 Ibid.

43 *Official Year Book of New South Wales 1945-1946* (New South Wales Government, Sydney, 1948), p.257,p.259.

(d)Further Consolidation of Federal Financial Control: 1940s-1970s

In 1946, Chifley obtained passage of the *States Grants (Tax Reimbursement) Act 1946* under which he continued the arrangement of providing the states with grants for the income tax that they would otherwise have raised. In financial year 1946-1947 he provided the states with £40,000,000 in grants. The share falling to New South Wales was £16,477,000, amounting around 22% of the state's revenue:

New South Wales Revenue 1946-1947[44]

Tax Reimbursement Grant	£16.4 million
Income from other Sources (incl. Business Undertakings)	£58.1 million
TOTAL	£74.5 million

Although a Liberal Party-Country Party government (led by Menzies) gained office at the end of 1949, Menzies initially kept the arrangements instituted by Curtin and Chifley. In financial year 1958-1959, the total amount of reimbursement grants provided to the states amounted to around £175 million: with New South Wales receiving about £65 million.[45] According to a later publication by the NSW Treasury, the formula used by the Commonwealth to calculate these grants, during the late 1940s and the 1950s, was as follows:

> The amount payable by the Commonwealth to the states was to be varied year to year, commencing 1948-1949, in accordance with changes in aggregate population and the level of wages throughout the Commonwealth.[46]

In 1959 Menzies amended the 1940s arrangements: obtaining passage of the *States Grants Act 1959* under which the former tax reimbursement grants were renamed financial assistance grants (FAGs). Menzies also amended the basis on which the grants were calculated, as the *Official Year Book of New South Wales* also explained:

> In 1960-1961 and each subsequent year, the grant payable to a state is to be determined by (a) multiplying the grant per head of population in the previous year by the population of the state on 1st July of the current year, and (b) increasing the resultant amount by 1.1 times the percentage by which the average wage per person employed in Australia in the previous year exceeds the average wage in the year before it.[47]

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44 Stargardt (ed.), p.212; *Official Year Book of New South Wales 1947-1948* (New South Wales Government, Sydney, 1950), pp.773,775.

45 Hugh Emy, *The Politics of Australian Democracy: Fundamentals in Dispute* (MacMillan, Melbourne, 1978), p.106.

46 NSW Treasury, *Introduction to Government Finance and Accounting in New South Wales* (NSW Treasury, Sydney, 1987), p.24.

47 *Official Year Book of New South Wales 1961* (New South Wales Government, Sydney,

In the first year of the financial assistance grant scheme, the FAG contributed just over 30% of the NSW budget:

New South Wales Revenue 1959-1960[48]

Financial Assistance Grant	£83.4 million
Income from other Sources (incl. Business Undertakings)	£179 million
TOTAL	£262.5 million

During the remainder of the 1960s and into the 1970s, the FAG proportion of NSW revenue rose even higher, increasing to around 40% in financial year 1970-1971:

New South Wales Revenue 1970-1971[49]

Financial Assistance Grant	\$486,739,000
Income from other Sources (incl. Business Undertakings)	\$760,510,000
TOTAL	\$1,247,249,000

Until the early 1970s, the federal government assistance grants were provided to the states with no conditions attached. In late 1972, Gough Whitlam became prime minister (leading an ALP government) with, as mentioned above, a platform of increasing the power of the Commonwealth to achieve social objectives. Whitlam's intention was to direct Commonwealth grants in such a way that they would be directly applied to specific purposes within the states. As he later recalled in his account of his government:

> What had never before been attempted was the use of. . .grants to achieve far-reaching reforms in education, medical services, hospitals, sewerage, transport and other urban and regional development programs.[50]

As well continuing to provide funds to the states to expend as they saw fit (funds which he now termed "general purpose" grants), Whitlam dramatically increased federal funding in the form of what he now called "specific purpose payments" (SPPs), as figures (from his own account of his administration) indicate:

1964), p.174.

48 *Official Year Book of New South Wales 1961*, pp.174,187-188.

49 *Official Year Book of New South Wales 1971* (New South Wales Government, Sydney, 1973), pp.173-174.

50 Gough Whitlam, *The Whitlam Government 1972-1975* (Viking, Melbourne, 1985), p.716.

Whitlam Government: General Purpose, and Specific Purpose, Payments to all States 1972-1975[51]

	1972-1973	*1973-1974*	*1974-1975*	*1975-1976*
General Purpose	$2.7 billion	$2.8 billion	$3.6 billion	$4.4 billion
Specific Purpose	$931 million	$1.5 billion	$2.9 billion	$4.1 billion

Social priorities were clearly reflected in the specific purpose payments, as illustrated by the following table of amounts:

Whitlam Government: Specific Purpose Payments to all States by Main Areas, 1972-1975[52]

	1972-1973	*1973-1974*	*1974-1975*	*1975-1976*
Education	$259.4 million	$622.9 million	$1.3 billion	$1.4 billion
Health	$21 million	$51.8 million	$108 million	$1 billion

By the early 1980s the proportion of Commonwealth grants, as a percentage of New South Wales revenue, remained at around 40% as the following table indicates:

Commonwealth Grants as a Percentage of NSW Revenue: 1960s-1980s[53]

1963	30%
1982	42%

5.THE ALP, THE LIBERAL AND NATIONAL PARTIES AND THE CONSOLIDATION OF COMMONWEALTH POWER

(a)The Trade Crisis of the late 1970s and early 1980s

During the 1980s a new direction emerged in the ALP's approach to national policy and national power. Rather than pursuing Commonwealth power to pursue social objectives, by the end of the 1980s the ALP had become pre-occupied with exerting the power of the Commonwealth for different purposes. The essence of this was later summarised by Paul Keating (ALP prime minister from late 1991 to 1996) in outlining the policies of the Hawke and (subsequent) Keating governments during 1983-1996:

> the Labor government embraced. . .market orientated policies. . .[as] the best way of ensuring the future of ordinary Australians. . .[our approach was on] opening the

51 Ibid., p.717.

52 Centre for Research on Federal Financial Relations, *1976 Report and Review of Fiscal Federalism in Australia* (Australian National University, Canberra, 1977), p.83.

53 Allan Barnard, "Government Finance" in Wray Vamplew (ed.), *Australians: Historical Statistics* (Fairfax, Syme and Weldon, Sydney, 1987), p.274.

> economy. . .[furthermore] Labor. . .[intended] to find new ways of delivering social justice. . .to compensate low income wage and salary earners. . .by providing government programs and payments to those who needed them.[54]

In 1973 Britain, hitherto by far the largest market for Australia's primary products, had joined the European Economic Community (EEC) and, as a consequence, had to apply protective tariffs to Australian agricultural commodities. Against the background of an already assured market for Australian agricultural products in England (through previously established tariff preferences), leading Australian politicians had also set out to use protective import duties to encourage the development of manufacturing. In the early 1900s Deakin, in his first term as prime minister, had overseen the introduction of the first schedule of protective import duties: labelling the program "new protection". In his second term as prime minister (1905-1908) he had overseen an additional schedule of protective import duties: covering 440 items with rates twice that of those fixed earlier. After the end of the First World War, Hughes's Nationalist Party government had established a Tariff Board to further the process of expanding Australian manufacturing through protective tariffs.[55] From the 1920s to the 1970s (just before Britain joined the EEC) successive Australian governments, on the advice of the Tariff Board, continued the imposition of protective duties. In financial year 1969-1970 the board reported that,

> The average rates of effective protection available to individual Australian manufacturing industries in 1967-1968 ranged from 0 to 120 per cent, and the average rate for manufacturing industry as a whole was 46 per cent.[56]

By the late 1970s the effects of Britain's joining the EEC soon became apparent. Butter exports declined from 79,000 tonnes in 1972-1973 to 7,000 tonnes in 1981-1982. Sugar exports to Britain (which had amounted to 500,000 tonnes in 1972) were virtually eliminated.[57] The number of beef cattle in Australia dropped from 33 million (in 1976) to 22 million (by mid 1983).[58]

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54 Paul Keating, "The Labor Government: 1983-1996", speech delivered at the University of New South Wales, 19 March 1999. Keating himself stated, in the early 1990s, that "I always believed that the private economy was the real generator of wealth". See Michael Gordon, *A Question of Leadership: Paul Keating Political Fighter* (University of Queensland Press, Brisbane, 1993), p.70.

55 Hancock, op.cit., in Scott (ed.), pp.499,507; F. Alexander, "Australia since the War" in Scott (ed.), p.618.

56 Alf Rattigan, *Industry Assistance: The Inside Story* (Melbourne University Press, Melbourne, 1986), p.78.

57 Bruce Davidson, "History of Farming" in National Farmers Federation (ed.), *Australian Agriculture*, fourth edition (Morescope Publishing, Melbourne, 1993), pp.43-44; Robert Hadler, "The Slide into Trade War" in *The Australian*, 16 November 1990, p.15.

58 Farmwide, *History of Beef in Australia* (Farmwide, Canberra, 2002), p.1.

At the same time that Australia began to feel the impact of Britain's membership of the EEC, an international downturn in production occurred: partly because of a decision, by a new revolutionary leadership in Iran, to dramatically increase the price of oil (causing it to rise from about $12 a barrel in 1974 to $34 a barrel in the early 1980s). Unemployment in Australia reached 6% in 1981 and 9.75% in early 1983.[59]

(b)The Hawke and Keating Governments: The Reduction of Government Control of Production and Commerce

In 1983, the Australian people once more elected an ALP government (led by Bob Hawke). As Frank Crowley observed, this was partly an outcome of the fact that "successive economic shocks had threatened the jobs, the businesses, the homes and the families of large numbers of Australians".[60] At this point in time however (because of the crisis in employment) the focus of the ALP, in relation to national power, shifted from pursuing it for social objectives to seeking it to further business. Hawke's solution to the loss of the British market for Australian agricultural produce, and to the international downturn in production, was twofold: closer integration of Australia into overseas production and commerce (on an international level), and advancing the prosperity and enlargement of Australian businesses (on a domestic level).

As far as the means to achieve these solutions was concerned, integrating Australia into international production and commerce entailed reducing tariff protection. Advancing the prosperity (and enlargement) of Australian businesses entailed laying the foundation for their operating on a national (rather than a state) level and facilitating their acquisition of undertakings that had, until then, been owned by governments.

Whereas, during the 1940s and the 1970s, it had been the policy of ALP governments (in the pursuit of social objectives) to shift power to the Commonwealth for the purposes of extending government control over production, the ALP now sought to shift power to the Commonwealth for the objective of removing government direction of production. As Graham Richardson (a former minister in the Hawke government) remarked to Stephen Martin (parliamentary speaker during the period of the subsequent Keating government), "That. . .[used to be] our raison d'etre. . .government control. When we got into government we ditched it immediately, which was a hell of a shock for a lot of people in the Labor party".[61]

In May 1987, Hawke issued an economic statement in which he inaugurated the sale of property and undertakings hitherto owned by the government. The first assets sold were land attached to the Australian embassy in Tokyo and mortgages held by the Defence

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59 Barrie Dyster and David Meredith, *Australia in the International Economy in the Twentieth Century* (Cambridge University Press, 1990), p.271.

60 Frank Crowley, *Tough Times: Australia in the Seventies* (Heinemann, Melbourne, 1986), p.418.

61 Stephen Martin, *Labor and Financial Deregulation: The Hawke/Keating Governments, Banking and New Labor* (PhD Thesis, University of Wollongong, 1999), p.163.

Services Housing Loans Corporation.[62] A year later, Hawke delivered another major economic statement in which, as John Madden has described, "major phased tariff cuts were announced. A continuation of this program [three years later]. . .meant that most nominal tariff rates were to be phased down to 5 per cent".[63]

On a state level, ALP governments began to evacuate government from areas into which their predecessors had earlier introduced it. In 1986 the Unsworth government obtained passage of the *Water Administration Act*. This legislation abolished the Water Resources Commission (which, ten year years previously, had replaced the Water Conservation and Irrigation Commission). The overall aim of the legislation was, as described by the then ALP minister for natural resources (Janice Crosio), to ensure that water was "allocated to the highest valued use".[64]

In 1991, Hawke announced that 30% of the Commonwealth Bank would be sold to business. It was also announced that the then Telecom Australia would lose its status as the single provider of telecommunications in Australia: ushering in Optus as a second fixed line network carrier and licensing Optus and Vodafone to be mobile phone carriers. Subsequently, after replacing Bob Hawke as prime minister in December 1991, Paul Keating oversaw the sale of even more government-owned assets: 25% of Qantas and Australian Airlines (financial year 1992-1993); 19% of the Commonwealth Bank (1993-1994); a management buyout of the Snowy Mountains Engineering Corporation (1993-1994); 19% of the Commonwealth Bank (1994-1995); 75% of QANTAS (1995-1996).[65]

Meanwhile, at the beginning of the 1990s, the ALP federal government (still led by Bob Hawke) embarked on strategy of drawing the states into closer association with national policy. As John Madden later outlined,

> Hawke invited the state premiers. . .to a series of special premiers conferences to undertake a review of intergovernmental relations in Australia. . .The federal government's primary motivation was to enable it to advance its. . .drive for

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62 Peter Walsh, *Confessions of a Failed Finance Minister* (Random House, Sydney, 1995), pp.162-165.

63 John Madden, *Australian Federalism Reforms and Global Integration* (Center for Research on Economic Development and Policy Reform, Stanford, 2002), pp.15-16.

64 Second Reading Speech, Water Administration Bill 1986. NSW Parliamentary Debates. Legislative Assembly. 13 November 1986, p.6397.

65 Geoff Hawker, "Ministerial Consultants and Privatisation: Australian Federal Government 1985-88" in the *Australian Journal of Politics and History*, vol.52, no.2, 2006, pp.250-252; Reserve Bank of Australia, *Privatisation in Australia* (Reserve Bank of Australia, Sydney, 1997); Nick Greiner, "Propaganda, Prejudice and Protests – Privatisation Policy in the 1990s" in Berna Collier and Sally Pitkin (eds.), *Corporatisation and Privatisation in Australia* (CCH Australia Limited, Sydney, 1999), p.3; Laura Tingle, *Chasing the Future: Recession, Recovery and the New Politics in Australia* (William Heinemann, Melbourne, 1994), p.210; OECD Economics Department, *Product Market Competition and Economic Performance in Australia* (Economics Department, Organisation for Economic Co-operation and Development, Paris, 2005), p.37.

> 'national efficiency and international competitiveness'. . .the intergovernmental review. . .marked a fundamental reshaping of Australia's federal system. . . intergovernmental committees at ministerial and official level have [since] for a decade worked towards policy and administrative solutions aimed at national approaches, removing interstate regulatory incompatibilities and interstate barriers.[66]

At the second special premiers conference, in 1991, Hawke gained significant concessions in the area of extending federal government control over state activities, and in the area of the transformation of state instrumentalities. In the realm of the extension of federal government control of state activities, an agreement was concluded under which the Commonwealth would have primary responsibility for public funding of higher education institutions while the states and territories would have responsibility for the establishment and oversight of such bodies. The conference also agreed that federal funds, provided directly to higher education institutions, would no longer be regarded as payments to the states and territories. This was an acknowledgment by the states and territories that provision of higher education in Australia had now become national in character.[67]

Co-operation with the state premiers, on the process of transforming state undertakings, was established formally in 1992 through the establishment of the council of Australian governments (COAG). This occurred, significantly, shortly after Keating delivered his *One Nation* policy statement.[68]

In 1993 Keating oversaw an agreement - between the federal government and the premiers of NSW, Victoria, Queensland and South Australia – to form an interstate electricity market. The conference concluded that state-owned electricity operations should be corporatised; that generation, transmission and distribution sectors in each state should be separated; that new investment would be subject to competitive tender by businesses; and that generation capacity in the states be divided into separate competing companies with open access to the transmission and distribution networks for new commercial generating facilities.[69]

In the same year that Keating inaugurated the new arrangements in electricity, he oversaw a COAG study on water policy: the report being prepared by a former chair of Westpac (Sir Eric Neal). When delivered a year later the report recommended, in regard to rural water

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66 Madden, op.cit., pp.14-15.

67 Australian Department of Education, Science and Training, *Rationalising Responsibility for Higher Education in Australia* (Australian Department of Education, Science and Training, Canberra, 2004), p.6.

68 Francis Castles and John Uhr, *Federalism and the Welfare State: Australia* (Australian National University, Canberra, 2002), p.48.

69 Productivity Commission, *Review of National Competition Policy Reforms* (Productivity Commission, Melbourne, 2005), pp.20,412; Sharon Beder and Damien Cahill, "Regulating the Power Shift: The State, Capital and Electricity Privatisation in Australia" in the *Journal of Australian Political Economy*, no.55, p.12.

provision, "changing pricing regimes to ensure that in time charges fully recoup operating costs".[70] COAG, as the Productivity Commission later described, subsequently "agreed to a strategic framework for water. . .to be implemented progressively through to 2001. The package sought. . .separation of water entitlements from land title. . .[and changes in] water allocation and trading."[71]

Simultaneously with the COAG negotiations on water, Keating concluded a similar agreement with the state premiers in regard to gas. The 1994 COAG agreement on gas provided for the separation of production, transmission, distribution and retailing of gas; the introduction of third party access regulation for natural gas pipelines; the removal of restrictions on trade in gas; and provision for all businesses to choose suppliers.[72]

A year later the overall process of change was officially given the name National Competition Policy.[73] In that year the Keating government obtained passage of the *National Competition Policy Reform Act 1995* which established the National Competition Council (NCC). The NCC proceeded to examine whether the various jurisdictions of the Commonwealth were meeting their obligations under national competition policy and related changes in areas such as electricity, gas and water.[74]

On gaining office federally (in 1996) the Liberal Party-National Party government, led by John Howard, initiated an NCP-related review of 1,800 pieces of Commonwealth and state legislation which had been identified as restricting competition.[75]

A year after gaining office, the Howard government obtained passage of the *Telecommunications Act 1997*. While Telstra (as Telecom Australia became) continued to remain the dominant provider (providing 70% of services offered over fixed line) the 1997 legislation laid the basis for the emergence of 100 companies owning specified infrastructure facilities and 1,000 service providers.[76]

In 1998 the National Electricity Market (NEM) began operations with New South Wales, Victoria and South Australia as the foundation members.[77] In 2001, Queensland joined the NEM and, three years later, COAG agreed to establish a single Australian Energy

70 Council of Australian Governments, *Water Resources Policy*, report of the Working Group on Water Resources Policy, February 1994, p.3.

71 Productivity Commission, *Review of National Competition Policy Reforms* p.421.

72 Ibid., p.416.

73 Madden, ibid.

74 OECD Economics Department, op.cit., p.26.

75 Ibid., p.27.

76 Ibid., p.38.

77 Beder and Cahill, op.cit., p.15.

Regulator (AER) and a new Australian Energy Market Commission (AEMC).[78]

In 2004, COAG endorsed the National Water Initiative (NWI) Agreement which, amongst other considerations, accepted the goal of national arrangements for trading in water.[79]

As well as launching the NWI, the Howard government inaugurated a new policy on land transport: Auslink. The aim of Auslink was to contribute to the development of an integrated national network of roads and railways. Auslink is to be implemented through a process of co-operation between the Commonwealth and state governments. Auslink is specifically intended to increase the amount of freight carried by promoting the integration of the different ways of transporting goods.[80]

6.COMMONWEALTH'S CONSOLIDATION OF FEDERAL STATE FINANCE

(a)The Extension of the Commonwealth Grants Commission's Role in Federal-State Funding: the Hawke and Keating Governments During the 1980s and 1990s

As part of laying the basis for furthering the prosperity of business, and in theory the nation, Bob Hawke (and his treasurer Paul Keating) set out to reduce taxation on companies. In the 1989-1990 budget, for example, the Hawke government reduced the rate of company tax from 49 cents in the dollar to 39 cents in the dollar.[81]

Reducing the tax on companies entailed significantly cutting public expenditure. As Russell Mathews and Bhajan Grewal remarked in 1995, "Between 1985-86 and 1989-90 the Commonwealth pursued the aim of drastically reducing public services".[82] Hawke's finance minister (Peter Walsh) wrote afterwards that,

> for the 1988-89 financial year. . .savings. . . [included] $850 million of payments to the states. . .When the 1989-90 budget was presented. . .The greater part of the. . . savings ($550 million) was a cut in grants to the states.[83]

In the 1990-1991 budget, Hawke made further savings of $400 million in grants to the states.[84]

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78 OECD Economic Department, op.cit., p.30.

79 Ibid., p.31.

80 Ibid., p.35.

81 Walsh, op.cit., p.189.

82 Mathews and Grewal, op.cit., p.24.

83 Walsh, op.cit., pp.189,213.

84 Don Nicholls, *Managing State Finance: The New South Wales* Experience (NSW Treasury, Sydney, 1991), p.122.

A significant innovation introduced by the Hawke government into federal-state finance, (made before the cuts to federal finance were begun) was to accept the role of the Commonwealth Grants Commission in determining the share of financial assistance between all the states and territories (a move initiated by the previous Fraser government). This potentially diverted criticism of the funding arrangements away from the Hawke government and towards the CGC. [85]

As a result of the cuts made by the Hawke government, between the mid 1980s and the early 1990s, the proportion of Commonwealth funding (as a percentage of overall NSW revenue) - which had risen to around 55% in 1985-1986 - returned by the early 1990s to the 1970s-1980s level of around 40% as the following table illustrates:

NSW Revenue: mid-1980s to early 1990s[86]

	1985-1986	*1990-1991*
Specific Purpose Payments	$4.8 billion	$4.7 billion
General Purpose Revenue Grants	$3.6 billion	$3.7 billion
Income from other Sources	$6.9 billion	$12.7 billion
TOTAL	$15.3 billion	$21.1 billion

A significant outcome of the Hawke government's cuts, to general purpose revenue grants, was that, as Grewal and Davenport have described, "specific purpose payments increased to more than 50 per cent of total net payments."[87] This is indicated by the following table for specific purpose payments to New South Wales in the early 1990s:

85 Commonwealth Grants Commission, *Equality in Diversity*, p.126; Groenewegen, op.cit., p.258.

86 *New South Wales Year Book 1988* (Australian Bureau of Statistics, Sydney, 1988), pp.412-215; *New South Wales Year Book 1993* (Australian Bureau of Statistics, Sydney, 1993), pp.238-245.

87 Peter Davenport and Bhajan Grewal, *The Australian Economy and Society: Shifting Boundaries of Social Welfare in the Australian Federation* (Centre for Strategic Economic Studies, Victoria University, Melbourne, 1997), p.5.

NSW Revenue: Federal Government Specific Purpose Payments 1990-1991[88]

Category	*Amount*
Education	$1.8 billion
Health	$1.3 billion
Economic Services	$583 million
Housing and Community Amenities	$309 million
General Public Services	$142 million
Social Security and Welfare	$134 million
Other Purposes	$358 million
TOTAL	$4.7 billion

During Paul Keating's term as prime minister (1991-1996), federal funding to the states was kept to a level of around 40%. The proportion of specific purpose payments, as a proportion of all federal funding to the states, increased to nearly 60% as indicated below:

NSW Revenue: 1994-1995[89]

Specific Purpose Payments	$5.8 billion
General Purpose Revenue Grants	$4.3 billion
Income from other Sources	$14.3 billion
TOTAL	$24.4 billion

A further development, in federal-state financial relations, was the introduction and subsequent elimination of federal payments to the states for the loss of income incurred when they sold off government-owned instrumentalities. The Keating government initially announced in 1992 that it would compensate the states for this loss of income and then, in 1993, declared that it would discontinue the process. This was denounced by all the state premiers: the ALP premier of Queensland (Wayne Goss) accusing the Keating government of "deceiving" the states and the Liberal Party premier of NSW (John Fahey) declaring that the Keating government was making the states come "begging" to the Commonwealth.[90]

(b)Impact of the Commonwealth Grants Commission

Only six years after Hawke drew the Commonwealth Grants Commission into deciding how FAGs should be divided between all the states, the influence of the CGC quickly became reflected in determinations that distributed the total amount of FAG funds away

88 Australian Bureau of Statistics, *New South Wales Year Book 1993* (Australian Bureau of Statistics, Sydney, 1993), p.245.

89 *New South Wales Year Book 1997* (Australian Bureau of Statistics, Sydney, 1997), pp.272-276.

90 Madden, op.cit., p.18; Michael Millett, "States Hit Hard over Asset Sales" in the *SMH*, 6 July 1993, p.1.

from the larger states and towards the smaller ones, as the following figures illustrate:

CGC Decisions on the Distribution of Financial Assistance Grants: 1992-1993[91]

State/Territory	*Population-Based Amount*	*CGC-Based Amount*	*Difference*
NT	$132,891,000	$782,000,000	+$649 million
Queensland	$2,393,475,000	$2,771,000,000	+$377 million
SA	$1,150,182,000	$1,521,000,000	+$371million
WA	$1,310,268,000	$1,587,000,000	+$277 million
Tasmania	$371,241,000	$578,000,000	+$207 million
ACT	$233,544,000	$372,000,000	+$138 million
Victoria	$3,513,609,000	$2,693,000,000	-$874 million
NSW	$4,707,627,000	$3,613,000,000	-$1 billion

(c)The Howard Government and the New Course of Financial Relations between the Commonwealth and the States

Not long after John Howard had become prime minister, following the election of a Liberal Party-National Party federal government in March 1996, Graeme Samuel (then the president of the Australian Chamber of Commerce and Industry or ACCI) declared that, although Howard had stated (in 1995) that he would "never, ever" place a goods and services tax (GST) on the political agenda, the ACCI considered that a GST had to "be on the agenda".[92]

The following year, the states lost a significant source of revenue when the High Court declared that business franchise fees were unconstitutional. To compensate the states, the Howard government proceeded to provide them with "revenue replacement payments" as David Collins has explained:

> [RRP]s were implemented as a result of the 1997 High Court decisions in the Ha and Lim v. NSW and Walter Hammond and Associates v. NSW cases, which effectively declared unconstitutional all state business franchise fees. These taxes, on alcohol, tobacco and petroleum, raised revenue [for all the states] of $5.221 bn. in 1996-7, their last year of operation. As a result of the potentially disruptive effects on state finances of such a revenue loss, the Commonwealth implemented 'safety net' arrangements. They consisted mainly of an increase in federal customs and excise duties on tobacco and alcohol. . .All revenue (less administrative costs) was returned to the states as RRPs. . .[93]

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91 Treasurer of the Commonwealth of Australia, *Budget Statements 1993-1994*, budget paper no.3 (Australian Government Publishing Service, Canberra, 1993), p.44. For population of Australia in 1992-1993 see Australian Bureau of Statistics, *Year Book Australia 1994* (Australian Bureau of Statistics, Canberra, 1993), p.118.

92 Ian Henderson, "GST – You Asked For It" in *The Australian*, 1 July 2000, p.38.

93 David Collins, *The Impact of the GST Package on Commonwealth-State Financial Relations* (Australian Tax Research Foundation, Sydney, 2000), p.26.

In 1998 the Liberal Party included a GST as part of its policy platform and presented it to the electorate in the federal election held in the same year. After being returned to office, in December 1998, the Howard government introduced legislation to provide for the introduction of a tax on goods and services: to be levied at a rate of 10%. GST revenue would be forwarded to the states, to essentially replace the former financial assistance grants and revenue replacement payments: conditional on either the removal or the downward adjustment of a number of state taxes (as worked out, between the Howard government and the premiers, in 1999).[94]

Meanwhile, by the end of the 1990s, federal funding (as a proportion of overall NSW revenue) had dropped from 40% to around 30%. More noticeably, the proportion of specific purpose payments, as a proportion of federal funding received by NSW, had dropped from 60% to just over 50% as the figures for 1998-1999 illustrate:

NSW Revenue: 1998-1999[95]

General Purpose Payments	$5.1 billion
Specific Purpose Payments	$5.5 billion
Income from other Sources	$19.6 billion
TOTAL	$28.9 billion

The individual specific purposes, and the funding allocated for financial year 1998-1999, were as follows:

94 Treasurer of the Commonwealth of Australia, *Budget Statement 2000-2001*, budget paper no.3, p.5; Treasurer of New South Wales, *Budget Statement 2000-2001*, budget paper no.3, p.16.

95 *New South Wales Year Book 2001* (Australian Bureau of Statistics, Sydney, 2001), pp.269-270; *Department of Finance and Administration, Final Budget Outcome1998-1999* (Department of Finance and Administration, Canberra, 1999), table 11.

NSW Revenue: Federal Government Specific Purpose Payments 1998-1999[96]

Category	*Amount*
Health	$2.1 billion
Education	$1.7 billion
Social Security and Welfare	$360 million
Transport and Communications	$336 million
Housing	$314 million
Public Order and Safety	$60 million
Agriculture, Forestry and Fishing	$57 million
Recreation and Culture	$4 million
Mining and Mineral Resources	$1 million
Other	$506 million
TOTAL	$5.5 billion

A continuous factor, contributing to the distribution of the GST revenue amongst all the states, was the Commonwealth Grants Commission: which the Howard government retained for this purpose (as the Hawke government had done) for the distribution of the financial assistance grants. The CGC based its conclusions on a system of comparative weightings between the states (known as "per capita relativities") derived from the following three considerations:

- calculation of the amount which a state would need to spend, in order to provide a national average level of public services

- calculation of the amount a state could raise, if it made a national average effort to raise revenue from its own resources

- calculation of the total assistance the state would require, to enable it to provide the national average of state-type services[97]

The weightings, calculated by the CGC for the first year of operation of the GST distribution, were as follows:

96 *Department of Finance and Administration, Final Budget Outcome1998-1999* (Department of Finance and Administration, Canberra, 1999), table 11.

97 David Collins, *The Impact of the GST Package on Commonwealth-State Financial Relations*, p.45.

Commonwealth Grants Commission Per Capita Relativities: 2000[98]

Northern Territory	4.16385
Tasmania	1.51091
South Australia	1.18258
ACT	1.11289
Queensland	1.01830
Western Australia	0.98365
New South Wales	0.90913
Victoria	0.87049

The outcome therefore, between a straightforward distribution of the GST revenue (on a per capita basis) and the eventual distribution (based on the CGC's weightings), was as follows for the first year of the GST's operation:

GST Revenue Distribution: Population-Based versus CGC-Based 2000-2001[99]

	Population	*Population-Based Share*	*CGC-Determined Share*	*Difference*
NSW	6,448,800	$8,351,196,000	$7,180,300,000	-$1.2 bn
VIC	4,753,900	$6,156,300,500	$5,027,300,000	-$1.1 bn
WA	1,877,500	$2,431,362,500	$2,337,800,000	-$94 m
NT	194,500	$251,877,500	$1,212,700,000	+$961m
TAS	470,300	$609,038,500	$971,900,000	+$363m
SA	1,496,100	$1,937,449,500	$2,247,700,000	+$310m
ACT	311,100	$402,874,500	$470,600,000	+$68m
QLD	3,549,300	$4,596,343,500	$4,604,100,000	+$8m

7.CONTESTS OVER SHARING OF THE GST REVENUE: COMMONWEALTH FUNDING AND NSW' OWN REVENUE

(a)Outcry from NSW Political Leaders

Ever since the first distribution of the GST revenue - in which New South Wales received over a billion dollars less (on a CGC basis) than it would have done on a pure population basis – there have been a steady stream of complaints from NSW leaders about the nature of the distribution. In 2004 the then premier of NSW, Bob Carr, announced that "We do not accept the formula" and described the five member commission as "a select priesthood of

98 Treasurer of the Commonwealth of Australia, *Budget Statement 2000-2001*, budget paper no.3, p.14.

99 Figures for the actual, CGC-based distribution, correspond to those from the Treasurer of NSW, *Budget Statement 2000-2001*, budget paper no.2, p.8-15. Population figures, for the calculation of population-based (or per capita) amounts, are from the Australian Bureau of Statistics, *Australian Demographic Statistics*, ABS Catalogue 3101 (Australian Bureau of Statistics, Canberra).

obscure and mediocre economists”.[100]

Essentially NSW premiers and treasurers have argued for the GST revenue to be distributed on a simple per head of population basis. A year following Carr’s outburst, his treasurer (Andrew Refshauge), referring to the 2005-2006 division of the GST revenue, declared that “Nothing can alter the fact that NSW, while it contributed $13 billion to total GST revenue, received only $10 billion back from the Commonwealth”.[101] Another year later, the current premier (Morris Iemma), expressed his view that the result of the CGC distribution amounted to “cheating” New South Wales: declaring that “There’s every indication that the cheating will continue, that there will be no fundamental change to the distribution of the GST.”[102]

(b)Continuing Shortfall on a Per Capita Basis

While retaining its role, in deciding the share of the GST revenue, the CGC continues to apply the principles of “fiscal equalisation” (equalising the revenue raising capacities of the states and territories) and “expenditure equalisation” (in which it attempts to equalise the expenditure effort, of the several jurisdictions, in delivering services). As outlined above, it puts these principles into effect by drawing comparisons between the various states and territories: assigning them weightings (“relativities”) prior to the division of the GST revenue. The CGC’s “relativities” for the states and territories, for 2005-2006, were as follows:

CGC Relativities for the States and Territories: 2005-2006[103]

Northern Territory	4.32765
Tasmania	1.54939
South Australia	1.18695
Australian Capital Territory	1.14585
Queensland	1.02404
Western Australia	1.00497
Victoria	0.89569
New South Wales	0.87346

100 The five member commission included, at that time, Ross Williams (former dean of the faculty of economics at Melbourne University) and Alan Morris (former head of the European Bank for Reconstruction and Development). See also Paolo Totaro, “Carr Fury over $376m Cut in Share of Tax Cake” in the *Sydney Morning Herald* (*SMH*), 3 April 2004, p.5.

101 Mike Steketee, “Carr’s New Stamp Duty Defies Costello” in *The Australian*, 25 May 2005, p.6.

102 Anne Davies and Matt Wade, “NSW Wins Crumb from the GST Pie” in the *SMH*, 2 March 2006, p.7.

103 Treasurer of the Commonwealth of Australia, *Budget Statement 2005-2006*, budget paper no.3.

On the basis of the above relativities, New South Wales once more received a less than per capita share of the GST revenue, as illustrated in the following table:

GST Revenue Shares: CGC Distribution v. per capita Distribution 2005-2006[104]

	CGC Distribution	*Per Capita Distribution*	*Difference*
Northern Territory	$1,832,700,000	$373,212,500	+$1.4 bn
South Australia	$3,449,000,000	$2,821,997,500	+$627 million
Tasmania	$1,501,400,000	$889,140,000	+$612 million
Queensland	$7,721,100,000	$7,301,825,000	+$419 million
ACT	$772,600,000	$596,227,500	+$176 million
Western Australia	$3,822,100,000	$3,702,377,500	+$119 million
Victoria	$7,864,500,000	$9,220,630,000	-$1.3 bn
New South Wales	$10,426,700,000	$12,415,475,000	-$1.9 bn

The above distribution for New South Wales in 2005-2006, compared with that for 2000-2001, shows that the percentage difference, between a CGC allotment versus a per capita distribution, has been increasing slightly:

CGC-Distribution, versus per capita Distribution, GST Revenue: 2000-01/2005-06

	PerCapita Distribution	*CGC Distribution*	*Percentage of Per Capita Share*
2000-2001	$8,351,196,000	$7,180,300,000	86%
2005-2006	$12,415,475,000	$10,426,700,000	84%

(c)New South Wales Government Revenue: Sources, and Usefulness, of Principal Taxes

Each year the New South Wales government requires an ever increasing amount of money to provide the level of service sought for by the community. The following table shows the increases in the state's budgets since the beginning of the new century:

104 See Neil Warren, *Benchmarking Australia's Intergovernmental Fiscal Arrangements* (New South Wales Government, Sydney, 2006), p.28. Per capita amounts derived by dividing total amount of GST revenue, provided in the Commonwealth treasurer's budget statement (budget paper number 3), by population figures in Australian Bureau of Statistics catalogue *Australian Demographic Statistics* (ABS catalogue 3101.0).

New South Wales Budgets: 2001-2002 to 2006-2007[105]

2000-2001	$30.4 billion
2001-2002	$32 billion
2002-2003	$36 billion
2003-2004	$37.7 billion
2004-2005	$39.2 billion
2005-2006	$41.2 billion
2006-2007	$42.2 billion

The most important sources, and the most useful sources, from which New South Wales derives its own revenue, can be listed as follows:

<u>Pay-Roll Tax</u>

Pay-roll tax is the most important source of tax for New South Wales. When a firm's wages bill is less than $600,000 no tax is payable. Over $600,000, the tax (in NSW) is levied at a rate of 6%. The increasing importance of the tax, in the constitution of state's revenue, can be seen in the increase of the amount levied between the late 1980s and the first years of the twentieth-first century:

New South Wales: Pay-Roll Tax Collected between late 1980s and early 2000s[106]

1987-1988	$1.8 billion
2003-2004	$4 billion

The usefulness of pay-roll tax to the state can be indicated by the increase in collections between financial year 2003-2004 and 2004-2005:

New South Wales: Pay-Roll Tax Collections 2003-2004 to 2004-2005[107]

2003-2004	$4.17 billion
2004-2005	$4.68 billion

<u>Stamp Duty</u>

As the median house has constantly increased in Sydney, particularly during the recent housing boom, the state government has been able to turn to stamp duty as an ever-important source of revenue. The rise in house prices, and the accompanying rise in stamp

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105 Treasurer of NSW, *Budget Statements 2000-2001* to *2006-2007*, budget paper no.2.

106 New South Wales Tax Task Force, *Review of the State Tax System* (NSW Government, Sydney, 1988), p.2; Treasurer of NSW, *Budget Statement 2003-2004*, budget paper no.2, chapter 3, p.13.

107 NSW Treasury, *New South Wales*: *Report on State Finances 2004-2005* (NSW Treasury, Sydney, 2005), p.3 – 23.

duty, can be shown as follows:

Median House Prices and Stamp Duties in Sydney: early 1980s to early 2000s[108]

	early 1980s	*early 1990s*	*2003*
Median House Price	$65,000	$180,000	$465,000
Stamp Duty	$1,065	$4,790	$16,000

Between the 1980s and the present, the amount of stamp duty levied in New South Wales – on conveyancing and other forms of transactions - has increased substantially as figures for the following selected years indicates:

New South Wales: Stamp Duty Collected, Selected Years late 1980s-early 2000s[109]

1986-1987	$1.3 billion
1987-1988	$1.9 billion
1992-1993	$2.4 billion
2003-2004	$5.5 billion

With the slow-down in the property boom, however, receipts from stamp duty have (overall) declined between 2003-2004 and 2004-2005 as figures from the NSW Treasury indicate:

New South Wales: Stamp Duty Collected 2003-2004 and 2004-2005[110]

2003-2004	$5.5 billion
2004-2005	$4.8 billion

The overall slow-down in revenue raising from stamp duty, since the beginning of the new century, has been outlined by Ross Williams as follows:

108 Real Estate Institute of Australia, *Submission to the Review of Commonwealth-State Funding* (Real Estate Institute of Australia, 2002), p.6; Peter Freeman, "Hard Pressed Home Buyers – Where the Blame Lies" in the *SMH*, 3 June 1992, p.33.

109 See NSW Tax Task Force, op.cit., p.2; "The State Budget", *SMH*, 8 September 1993, p.13; NSW Treasury, *New South Wales: Report on State Finances 2004-2005*, p.3-23.

110 NSW Treasury, *New South Wales: Report on State Finances 2004-2005*, p.3-23.

New South Wales: Reduced Revenue Raising Capacity from Stamp Duty, 1999/2000 to 2003/04 (Australian Average=1.00)[111]

1999-2000	1.33
2000-2001	1.35
2001-2002	1.34
2002-2003	1.3
2003-2004	1.2

Gambling Tax

Because of the relatively higher amounts lost by people in NSW on gambling - $1,211 per capita during 2001-2002 –New South Wales has been able to levy the second-highest amount of gambling tax amongst the states and territories ($318 per capita in 1999-2000).[112]

On a general level, the share of gambling revenue, in total NSW revenue, has declined over the years as the table below illustrates:

New South Wales: Gambling Revenue as a %age of State Taxation 1970/71-1995/96[113]

1970-1971	19%
1975-1976	13%
1980-1981	14%
1985-1986	11%
1990-1991	10%
1995-1996	10%

Despite the proportion of gambling tax, in overall state revenue, declining between the 1970s and the 1990s, the amount of tax levied by the state, on poker machines and racing, still remains significant as indicated by the following table:

111 Ross Williams, *Fiscal Federalism: Aims, Instruments and Outcomes*, p.24.

112 See Tasmanian Gaming Commission, *Australian Gambling Statistics 1974-1975 to1999-2000*.

113 Julie Smith, *Australian Gambling Taxation* (Economics Program, Australian National University, Canberra, 1999), p.11.

New South Wales: Gambling Tax Collected, Selected Years late 1980s to mid-2000s[114]

1986-1987	$397 million
1987-1988	$442 million
1992-1993	$942 million
2003-2004	$1.3 billion
2004-2005	$1.6 billion

Land Tax

Land tax was introduced in the mid-1950s, by the then ALP state government in NSW (led by Joe Cahill) when it obtained passage of the *Land Tax Act 1956*. It was then described as a "tax on the unimproved capital value of freehold lands in New South Wales".[115] It has recently been described, by Ross Gittins, as "a tax on investment properties".[116] Two years after gaining office (in 1995), the ALP state government (led by Bob Carr) obtained passage of the *State Revenue Legislation Amendment Act 1997*. Under this legislation, the rate of land tax was increased by 0.2% and the levy itself became applied to principal places of residence with a value over $1 million.[117] In 2004 the Carr government extended the tax to all second properties. A year later, with Morris Iemma heading the ALP state government, the commencement point of the levy was reviewed: to begin when the value of the land, belonging to a second property, reached $330,000.[118]

In recent years, an ever-increasing amount of revenue has been levied through land tax, as shown accordingly:

114 New South Wales Tax Task Force, op.cit., p.2; "The State Budget", *SMH*, 8 September 1993, p.13; NSW Treasury, *New South Wales: Report on State Finances: 2004-2005*, p.3 – 23.

115 *The Official Year Book of New South Wales 1959* (NSW Government, Sydney, 1961), p.283.

116 Ross Gittins, "Why You're Hating the Wrong State Taxes" in the *SMH*, 5 June 2003, p.44.

117 NSW Legislative Council (General Purpose Standing Committee No.1), *Report on the Inquiry into Changes in Land Tax in New South Wales* (NSW Parliament, Sydney, 1998), p.1.

118 Anne Davies and John Garnaut, "Out with the Old Land Tax Regime, in with the New" in the *SMH*, 31 December 2005, p.4.

New South Wales: Land Tax Collected, Selected Years late 1980s to early 2000s[119]

1985-1986	$296 million
1986-1987	$345 million
1987-1988	$413 million
1992-1993	$477 million
1997-1998	$856 million
1998-1999	$946 million
2003-2004	$1.3 billion

The usefulness of land tax to the state is illustrated by the fact that, whereas the amount of stamp duty revenue collected by NSW declined between 2003-2004 and 2004-2005, the state was able to levy an increased amount of land tax between the same two years:

New South Wales: Land Tax Collected 2003-2004 and 2004-2005[120]

2003-2004	$1.3 billion
2004-2005	$1.6 billion

Taxes on Motor Vehicles

According to the Organisation for Economic Co-operation and Development, motor vehicle tax accounts for around 10% of the revenue raised by NSW on its own behalf.[121] With the constant increase in population, motor vehicle tax provides a source of revenue that increases (if only slightly) each year, as the following table indicates:

New South Wales: Motor Vehicle Tax Collected 2003-2004 and 2004-2005[122]

2003-2004	$1.1 billion
2004-2005	$1.25 billion

(d)Specific Purpose Payments to New South Wales

Specific purpose payments to the states were maintained, parallel to the distribution of the GST revenue, during the years 2000-2001 to 2004-2005 and payments to New South Wales

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119 NSW Treasury, *Introduction to Government Finance and Accounting in New South Wales*, p.30; New South Wales Tax Task Force, op.cit., p.2; "The State Budget" in the *SMH*, 8 September 1993, p.13; NSW Legislative Council (General Purpose Standing Committee No.1), op.cit., p.75, NSW Treasury, *New South Wales: Report on State Finances: 2004-2005*, p.3 – 23.

120 NSW Treasury, *New South Wales: Report on State Finances 2004-2005*, p.3-23.

121 Organisation for Economic Co-operation and Development, *Economic Survey: Australia 2006* (OECD, Paris, 2006), p.88.

122 Treasurer of New South Wales, *Budget Statement 2003-2004*, budget paper no.2; *Budget Statement 2004-2005*, budget paper no.2.

actually increased. As the CGC reported this year,

> New South Wales's share of SPPs increased between 1999-2000 and 2004-2005, particularly its share of the Auslink-State roads component and government schools payments.[123]

The specific purpose payments received by New South Wales, for 2004-2005, were as follows:

NSW Revenue: Federal Government Specific Purpose Payments 2004-2005[124]

Category	*Amount*
Health	\$3 billion
Education	\$2.8 billion
Social Security	\$0.6 billion
Transport	\$0.6 billion
Housing	\$0.3 billion
Agriculture	\$0.1 billion
Fuel	\$31 million
Public Order	\$5 million
Recreation	\$1 million
Other	\$0.6 billion
TOTAL	\$8 billion

8.SURVEYING THE CONSIDERATIONS IN NSW' CLAIMS

(a)Wealth of the State

In any consideration of the distribution of GST revenue, the wealth of the state is a crucial factor. Indeed, in past years, it has been the boast of state governments that New South Wales is the most prosperous state in Australia. In 1959, for example, the NSW government produced a book on the state, the opening page of which declared that,

> New South Wales. . .remains the leader in population, wealth, industry, and social and economic development. The state has more than one-third of Australia's 10 million inhabitants. The annual revenue from its primary and manufacturing industries – over £1,000m – is some 40 per cent of Australia's total.[125]

123 Commonwealth Grants Commission, *Report on State Revenue Sharing Relativities: 2006 Update* (Commonwealth Grants Commission, Canberra, 2006), p.42.

124 *Department of Finance and Administration, Final Budget Outcome2004-2005* (Department of Finance and Administration, Canberra, 2005), table 36.

125 NSW Government, *New South Wales, Australia* (NSW Government, Sydney, 1959), p.5.

New South Wales continues to lead the states and territories in output: one broad indication of which is gross state product or GSP (a measurement of the volume of goods and services produced in a state). The GSP figures, for 2004-2005, were as follows:

Australian States and Territories: Gross State Product 2004-2005[126]

State/Territory	*Gross State Product*	*Percentage Australian GDP*
New South Wales	$294 billion	33%
Victoria	$221.5 billion	25%
Queensland	$166.2 billion	19%
Western Australia	$89.8 billion	10%
South Australia	$62.3 billion	7%
Australian Capital Territory	$28.2 billion	3%
Tasmania	$18.2 billion	2%
Northern Territory	$12 billion	1%
TOTAL (AUSTRALIA GDP)	$892 billion	

Another indication of the wealth of New South Wales is its share of net private sector wealth. In 2005 the total value of national net private sector wealth amounted to around $6,215 billion. On an approximate level, this equated to about $305,000 per capita. On this basis, the share of net private sector wealth, belonging to NSW, was about 33% as the accompanying table illustrates:

Australia: Net Private Sector Wealth 2004-2005 approx. (State Populations x National Per Capita Amount of $305,000)[127]

New South Wales	$2,069 billion (33%)
Victoria	$1,535 billion (25%)
Queensland	$1,204 billion (20%)
Western Australia	$616 billion (10%)
South Australia	$473 billion (8%)
Tasmania	$151 billion (2%)
Australian Capital Territory	$102 billion (1½%)
Northern Territory	$65 billion (½%)
TOTAL	$6,215 billion

The greatest amount of net private sector wealth is held in houses or apartments. The share of this form of wealth, as a proportion of total national wealth, is about 58%:

126 Australian Bureau of Statistics, *Australian National Accounts: State Accounts 2004-2005*, ABS Catalogue 5220.0 (Australian Bureau of Statistics, Canberra, 2005).

127 Australian Treasury, *Economic Roundup: Summer 2006* (Australian Treasury, Canberra, 2006), p.90.

Australia: Proportion of Net Private Sector Wealth Held in Houses and Apartments 2004-2005 (approx.)[128]

Total National Private Sector Wealth	$6,215 billion
Proportion of Wealth Held in Houses and Apartments	$3,605 billion (58%)

Sydney, amongst all the capital cities in Australia, obtains the highest median prices for houses, as well as the highest individual prices. The median houses prices for the various capital cities, in 2005, were as follows:

Australia: Capital City Median House Prices 2005[129]

Sydney	$523,000
Perth	$455,000
Canberra	$424,000
Melbourne	$352,000
Brisbane	$339,000
Darwin	$332,000
Adelaide	$321,000
Hobart	$243,000

A comparison of luxury house prices, in Sydney and Melbourne in 2000, shows that (at that time) prestige houses in Sydney were selling for almost twice the price of equivalent dwellings in Melbourne:

Sydney: Top Five Auction Sale Prices in 2000[130]

Vaucluse	$7.4 million
Vaucluse	$6 million
Point Piper	$5.78 million
Point Piper	$5.5 million
Mosman	$5.15 million

128 Ibid., p.92.

129 Press Release. Australian Property Monitors, *Upswing in National House Prices Including Sydney*, 1 August 2006.

130 www.homepriceguide.com.au

Melbourne: Top Five Auction Sale Prices in 2000[131]

South Yarra	$3.825 million
Armadale	$3.425 million
Armadale	$3.035 million
Brighton	$2.915 million
Kew	$2.810 million

(b)Expenditure Difficulties of Other States and Territories

The most fundamental consideration, in the CGC's basis for sharing GST revenue, is how much it costs each of the states, and territories, in providing services. For 2005, expenditure levels (per capita) can be estimated on the basis of a table produced by Ross Williams (an economist adviser on the CGC):

State and Territory Levels of Expenditure (per capita) in Providing Services: 2003-2004[132]

	NT	*ACT*	*SA*	*WA*	*TAS*	*NSW*	*VIC*	*QLD*
Education	$2,673	$1,784	$1,593	$1,901	$1,650	$1,526	$1,508	$1,463
Health	$2,527	$1,617	$1,652	$1,502	$1,300	$1,439	$1,450	$1,232
Transport	$1,141	$498	$338	$316	$467	$626	$675	$542
Public Order	$1,306	$674	$653	$416	$546	$581	$502	$542
Social Security	$462	$427	$378	$278	$410	$431	$402	$231
Housing	$211	$501	$372	$401	$306	$212	$224	$226
Recreation	$1,141	$294	$176	$142	$225	$139	$150	$147
Agriculture	$246	$6	$184	$113	$254	$104	$84	$168
TOTAL	$9,707	$5,801	$5,346	$5,069	$5,058	$5,058	$4,995	$4,559

(c)The Capacity of the States and Territories to Raise Revenue

Another important element, in calculating the apportionment of GST revenue, is the capacity of the each state and territory to raise revenue. This capacity has been examined by the Commonwealth Grants Commission over many years. In a recent paper, a secretary of the CGC (Bob Searle) explained the essence of the CGC's calculations as follows:

> the. . .commission. . .[compares] the revenue each state would raise from its own sources, if it made the same revenue as all the other states. . .It is what they would collect if they each imposed taxes at the average rate. . .[133]

131 Ibid.

132 Williams, op.cit., p.16.

133 Bob Searle, *Federal Fiscal Relations in Australia* (International Centre for Economic Research, Turin, 2002), pp.22-23.

In the year that the GST was introduced, the CGC produced another of its estimations of what revenue (per head of population) the states and territories *could* produce (if they imposed state taxes at the average rate) compared to the revenue that they *actually* did produce:

Australian States and Territories: Total Amount Own-Source Revenue (per capita) compared to CGC-Standardised Amount 1999-2000[134]

	Actual Revenue Raised per Capita	*Revenue That Could Be Raised per Capita (as Estimated by CGC)*
NSW	$1,994	$2,150
VIC	$2,148	$1,977
QLD	$2,084	$1,915
WA	$1,897	$2,274
SA	$2,002	$1,674
ACT	$1,667	$1,771
NT	$1,506	$1,809
TAS	$1,284	$1,470

(d)Expenditure on Services and Revenue Raising Capacity

A comparison of the types of tables in subsections (b) and (c) above illustrates more concisely the difficulties encountered by the different jurisdictions:

Australia: States and Territories Expenditure on Services v. Revenue Raising Capacity (on per capita basis) 2003-2004[135]

State/Territory	*Expenditure on Services (per capita)*	*CGC Estimated Revenue (per capita)*	*Actual Revenue Raised Per Capita*
Northern Territory	$9,707	$1,897	$1,854
ACT	$5,801	$2,003	$1,955
South Australia	$5,346	$1,770	$1,971
Western Australia	$5,069	$2,587	$2,877
Tasmania	$5,058	$1,474	$1,581
New South Wales	$5,058	$2,425	$2,415
Victoria	$4,995	$2,048	$2,061
Queensland	$4,559	$2,265	$2,062

134 Ibid., p.28.

135 Figures on expenditure on services (per capita) from Williams, op.cit., p.16; figures for actual, and CGC-estimated revenue (per capita) from Commonwealth Grants Commission, *2006 Update Working Paper: State Finances – Report on State Revenue Sharing Relativities*, vol.2 (Commonwealth Grants Commission, Canberra, 2006), pp.13,16.

Of all the states and territories, in the above table, Queensland obviously stands out: in terms of being the state that has the lowest expenditure on services but equally raises significantly less in revenue (per capita) than other jurisdictions.

The Northern Territory also attracts attention: in relation to the contrast between its receipts of GST revenue and the amount it actually expends on services. In an article entitled "Labor Delivers More of the Same to NT Aborigines", Mike Steketee (writing in *The Australian*) recently commented that "A count of the bottom dollar shows that the Martin government hasn't put its money where its mouth is on financial support for indigenous communities".[136]

The criticisms of the NT's expenditure call into question the essence of the CGC's basis for calculating the shares of the GST. In the mid-1990s, Richard Rye (then chair of the CGC) and Bob Searle (then CGC secretary) provided the following case for shifting the balance of distribution away from the New South Wales and Victoria and towards the NT:

> About one-quarter of the territory's population is indigenous Australian Aborigines. The costs of providing schools, medical and other services to Aboriginal settlements in remote, often semi-desert, areas are very high. All in all, the territory's relative per-capita cost of service provision is nearly three times the average for the other states.[137]

In its analyses of the financial requirements – contrasted with the expenditure needs - of the various states and territories, the CGC prepares yearly assessments of what it believes the various jurisdictions could be expected to spend (against what they do in practice). In certain areas the NT spends more on services than the CGC judges requisite. This can be seen as follows:

NT Expenditure against CGC-Assessed Expenditure Levels: Selected Areas 2004-05[138]

	NT Expenditure	*CGC Assessment*
Culture and Recreation	$107 million	$36 million
Population and Preventative Health Services	$110 million	$43 million
Manufacturing and other Industry	$75 million	$6 million
Electricity and Gas	$40 million	$11 million
Primary Industry	$38 million	$25 million

136 Mike Steketee, "Labor Delivers More of the Same to NT Aborigines" in *The Australian*, 21 September 2006, p.12.

137 Richard Rye and Bob Searle, "The Fiscal Transfer System in Australia" in Ehtisham Ahmad (ed.), *Financing Decentralised Expenditures: An International Comparison of Grants* (Edward Elgar, Cheltenham, 1997), p.158.

138 Commonwealth Grants Commission, *Report on State Revenue Sharing Relativities 2006 Update: Working Papers 2000-2001 to 2004-2005*, vol.3, *Assessment Results Expense* (Commonwealth Grants Commission, Canberra, 2006), pp.335, 545, 570, 699, 736.

In other areas, the NT spends less than the CGC assessment. This is also indicated as follows:

NT Expenditure against CGC-Assessed Expenditure Levels: Selected Areas 2004-05[139]

	CGC Assessment	*NT Expenditure*
Inpatient Services	$265 million	$248 million
Government Primary Schools Education	$211 million	$202 million
Non-Inpatient and Community Health Services	$202 million	$163 million
Services to Indigenous Communities	$163 million	$95 million
Government Secondary Schools Education	$149 million	$115 million
Housing	$124 million	$106 million
Family and Child Services	$123 million	$45 million
Homeless and General Welfare	$60 million	$1 million
Water, Sanitation and Environment Protection	$32 million	$3 million
Transport of Rural School Children	$13 million	$2 million

CONCLUSION

The premier of this state, in August of this year, declared (in a speech distributed to reporters) that, as far as relations between the states and the national government were concerned, there should be "Change that either reinforces the autonomy and the funding bases of the states or. . .[change that] puts them out of their misery by shifting Australia to a unitary system of government".[140] A survey of party policy in Australia, over the last century, indicates however that a form of unitary decision-making (if not a unitary state) has already begun to develop in Australia.

Originally the Australian Labor Party favoured centralised control: for the sake of pursuing a program of social objectives. Subsequently, after being out of power in the second half of the 1970s, the ALP proceeded to employ central control to enhance the progress of the market in Australia: as an alternative way of achieving the same purposes as its predecessors. After its election in 1996, the Howard government has (by and large) retained the same commitments.

Currently, businesses that were state-based now operate on a national level. Thus in 2004, in the realm of electricity and gas operations, NSW-based companies (such as Origin and AGL) have a substantial presence in Victoria. Origin had 36% of the total number of customers for electricity - and 35% of the total number of customers for gas – in that state. AGL had 36% of the total number of customers for electricity – and 33% of the total number of customers for gas – in Victoria.[141]

139 Ibid., pp.112, 197, 258, 275, 321, 347,401, 415, 434, 583.

140 Brad Norington and Imre Salusinszky, "Push For States to Run GST" in *The Australian*, 5 August 2006, p.7.

141 Essential Services Commission, *Review of Effectiveness of Retail Competition and Consumer Safety Net in Gas and Electricity* (Essential Services Commission, Melbourne, 2004), p.24.

Since, particularly through national competition policy, Australia is moving closer to functioning on a national basis, it does not seem entirely unreasonable that, in the realm of federal-state finance, some assistance is afforded those areas of the nation where services are more costly to provide. Thus it would not seem out of the question for other areas of Australia to provide some form of subsidy to Tasmania and South Australia which appear to have a certain amount of difficulty in delivering services. On the other hand, it seems equally reasonable to assert that, if another area of the nation not only spends less on service delivery than others, but also raises less revenue on average, then that part of the nation should receive less than its current share of funding. In point of fact this would appear to mean Queensland. Indeed the treasurer of that state has, in the past, acknowledged this, declaring (in his budget statement) that,

> Queensland's taxation revenue raising effort, as assessed by the Commonwealth Grants Commission, has remained below the Australian policy standard (equal to 100%) for some time.[142]

It would also seem reasonable to assert that if another jurisdiction in the nation receives a proportionally larger share of GST revenue, and then declines to expend it in full – in the very areas which led the CGC to conclude that extra funding was warranted in the first place – then there might be a case for a review of that jurisdiction's portion of federal funding. This may be so in the case of the Northern Territory.

142 Treasurer of Queensland, *State Budget 2003-2004*, budget paper no.2, p.72.

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