



THIRTY-SEVENTH PARLIAMENT

REPORT 13
STANDING COMMITTEE ON ESTIMATES AND
FINANCIAL OPERATIONS
ANNUAL REPORT 2007

Presented by Hon Giz Watson MLC (Chair)

June 2008

STANDING COMMITTEE ON ESTIMATES AND FINANCIAL OPERATIONS

Date first appointed:

30 June 2005

Terms of Reference:

The following is an extract from Schedule 1 of the Legislative Council Standing Orders:

“2. Standing Committee on Estimates and Financial Operations

- 2.1 An *Estimates and Financial Operations Committee* is established.
- 2.2 The Committee consists of 5 Members, 3 of whom shall be non-government Members.
- 2.3 The functions of the Committee are to consider and report on -
- (a) the estimates of expenditure laid before the Council each year;
 - (b) any matter relating to the financial administration of the State;
 - (c) any bill or other matter relating to the foregoing functions referred by the House;
 - (d) to consult regularly with the Auditor General and any person holding an office of a like character.”

Members as at the time of this reporting period:

Hon Giz Watson MLC (Chair)	Hon Ken Travers MLC (Deputy Chair)
Hon Shelley Archer MLC (1 January 2007 to 20 March 2007)	Hon Sheila Mills MLC (appointed 1 May 2007)
Hon Anthony Fels MLC (1 January 2007 to 4 December 2007)	Hon Helen Morton MLC (appointed 28 June 2007)
Hon Brian Ellis MLC (appointed 5 December 2007)	Hon Nigel Hallett MLC (1 January 2007 to 28 June 2007)

Staff as at the time of this reporting period:

Lisa Peterson, Advisory Officer (General)	Carolyna Malouf, Committee Clerk
Renaë Jewell, Committee Clerk, (January 2007 to December 2007)	Lisa Parrella, Committee Clerk (December 2007)

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REPORT OF THE STANDING COMMITTEE ON ESTIMATES AND FINANCIAL OPERATIONS

ANNUAL REPORT 2007

1 INTRODUCTION

- 1.1 This report provides an overview of the work of the Standing Committee on Estimates and Financial Operations (**Committee**) conducted during the third year of the Thirty-Seventh Parliament, between 1 January 2007 and 19 December 2007 (**report period**).

History and Purpose

- 1.2 On 30 June 2005 the Legislative Council (**Council**) appointed the Committee. The Committee is a standing committee, which means that its existence is not linked to a particular inquiry or to a particular time period and it continues until the Council decides otherwise.
- 1.3 Scrutiny of the estimates of expenditure and the financial operations of government is a major function of the Council. Since the establishment of the modern Legislative Council committee system in 1989, this function has been the responsibility of both standing finance committees (such as the Committee) and *ad hoc* Budget review committees (such as annually constituted estimates committees).
- 1.4 Review of the committee system in 1997 and again in 2005 led to changes in the area of the Council's consideration of the annual estimates of expenditure and the financial operations of Government, the most recent changes being reflected in the appointment of the Committee.
- 1.5 The functions of the Committee are to consider and report on matters relating to the estimates of expenditure laid before the Council each year and the financial administration of the State. The Committee's terms of reference are extremely broad, enabling the Committee to initiate investigations relating to any aspect of the financial administration of the State. This includes inquiry into any matter relating to past, current, proposed and future expenditure by the public sector.
- 1.6 The terms of reference of the Committee are:¹

2. *Estimates and Financial Operations Committee*

- 2.1 *An Estimates and Financial Operations Committee is established.*

¹ Schedule 1, Standing Orders of the Legislative Council.

2.2 *The Committee consists of 5 Members, 3 of whom shall be non-Government Members.*

2.3 *The functions of the Committee are to consider and report on -*

- (a) the estimates of expenditure laid before the Council each year;*
- (b) any matter relating to the financial administration of the State;*
- (c) any Bill or other matter relating to the foregoing functions referred by the House; and*
- (d) to consult regularly with the Auditor General and any person holding an office of a like character.*

Membership

1.7 The Committee comprises five Members of Parliament appointed by the Council. During the report period a number of changes were made to the membership of the Committee:

- i) On 20 March 2007 Hon Shelley Archer MLC resigned from the Committee.
- ii) On 1 May 2007 Hon Sheila Mills MLC was appointed as a Member of the Committee, replacing Hon Shelley Archer MLC.
- iii) On 9 May 2007 the Committee granted Hon Anthony Fels MLC leave of absence from the Committee until the Select Committee of Privilege on a Matter Arising in the Standing Committee on Estimates and Financial Operations (**Select Committee of Privilege**) reported. The Select Committee reported on 13 November 2007.
- iv) On 28 June 2007 by resolution of the Council, Hon Helen Morton MLC replaced Hon Nigel Hallett MLC as a Member of the Committee.
- v) On 4 December 2007, by order of the Council, Hon Anthony Fels MLC was removed as a Member of the Committee, the Council adopting the recommendation of the Select Committee of Privilege that Hon Anthony Fels MLC not serve on any committee for the rest of the session.
- vi) On 5 December 2007 by resolution of the Council, Hon Brian Ellis MLC was appointed as a Member of the Committee, replacing Hon Anthony Fels MLC.

- 1.8 At the end of the report period the Committee comprised the following Members: Hons Giz Watson (Chair), Ken Travers (Deputy Chair), Sheila Mills, Helen Morton and Brian Ellis MLCs.
- 1.9 It is significant to note that the Committee is required by the Standing Orders of the Council to have a non-Government majority.²

Staff

- 1.10 The Committee is supported by the Legislative Council Committee Office. During the report period the Committee was staffed by: Lisa Peterson, Advisory Officer (General); Renae Jewell, Committee Clerk; and Lisa Parrella, Committee Clerk.
- 1.11 Dr Colin Huntly, Advisory Officer (Legal) and Ms Lavina Cheong, Articled Clerk, assisted the Committee with its inquiry into the Balga Works Program.
- 1.12 The Committee extends its thanks to the staff of the Legislative Council Committee Office for their valuable assistance.

2 ACTIVITIES OF THE COMMITTEE DURING THE REPORT PERIOD

Estimates of Expenditure Review - 2007/08 Budget Estimates

- 2.1 Government revenue goes into the Consolidated Account³, which is the major source of funding for the State public sector.⁴ The 'estimates of expenditure' comprise the Appropriation (Consolidated Account) Bills and the supporting documentation (**Budget Papers**). On an annual basis these are presented to Parliament in order that Government may access or 'appropriate' money from the Consolidated Account to fund expenditure by the Government over a given financial year.⁵
- 2.2 It is a function of the Committee to consider and report on the estimates of expenditure laid before the Council each year.
- 2.3 Historically in the Legislative Council annual budget estimates hearings were held over three to four days during which Members could ask questions relating to the Budget Papers. This has always provided an opportunity for the involvement of all Members of the Council not just the Members of a particular committee. Noting various criticisms about this process, the Committee has adopted an innovative

² Western Australia, Legislative Council, *Parliamentary Debates (Hansard)*, 30 June 2005, p3730.

³ Subsequent to the assent of the *Financial Management Act 2006* on 21 December 2006, the Consolidated Fund is now called the Consolidated Account.

⁴ The major revenue sources for the Western Australian Government include taxes, imposts, fines, rates, duties, royalties and Commonwealth Government grants: section 64, *Constitution Act 1889*, and section 8 of the *Financial Management Act 2006*.

⁵ Section 72, *Constitution Act 1889*.

procedure for the examination of the annual estimates of expenditure whereby the Committee holds estimates hearings throughout the year (**Ongoing Hearings**), as well as holding hearings on one to three consecutive days after the Budget Papers are tabled in the Council (**Annual Hearings**).

Annual Hearings

2.4 The Annual Hearings were held on 21 June 2007. The Committee heard from the following agencies (or parts thereof):

- Department of Education and Training
- Curriculum Council
- Department of Housing and Works; Housing Authority
- Department of Local Government and Regional Development
- Department of Child Protection
- Department of Communities
- Water and Rivers Commission/Department of Water
- Department of Environment and Conservation
- Main Roads Western Australia

2.5 All Members of the Council were notified of the hearings and invited to participate.

2.6 All of the hearings were public and the proceedings were recorded by *Hansard*. Full transcripts of evidence taken at the hearings can be found at the Committee's web page.⁶

2.7 The Committee refers readers to its report in relation to the 2007/08 annual budget estimates hearings for further information.⁷

Ongoing Hearings

2.8 The Committee conducted Ongoing Hearings in relation to the 2007/08 Budget in August, September, October, and December 2007. The agencies which the Committee heard from are listed in table 1 below.

⁶ <http://www.parliament.wa.gov.au/web/newwebparl.nsf/iframewebpages/Committees+++Current> (current at 25 June 2008).

⁷ Western Australia, Legislative Council, Standing Committee on Estimates and Financial Operations, Report 10, *Annual Hearings in Relation to the Budget Estimates 2007/08*, September 2007.

Table 1**Ongoing Budget Estimate Hearings**

Date	Agency
27 August 2007	Fremantle Port Authority
	Western Australian Land Authority
	Department of Planning and Infrastructure
3 September 2007	Department of Health
17 September 2007	Department of Corrective Services
22 October 2007	Department of Culture and the Arts
10 December 2007	Department of the Legislative Council
	Parliamentary Services Department

- 2.9 All Members of the Council were notified of the hearings and invited to participate.
- 2.10 All of the hearings were public and the proceedings were recorded by *Hansard*. Full transcripts of evidence taken at the hearings can be found at the Committee's web page.⁸

Issues arising out of the hearing with the Western Australian Sports Centre Trust

- 2.11 On 30 October 2006 the Committee held a hearing with the WA Sports Centre Trust (**Trust**) as part of its consideration of the 2006/07 Budget Estimates. Issues arose out of that hearing relating to two agreements entered into by the Trust, which the Committee referred to the Auditor General for advice.
- 2.12 The referral was undertaken pursuant to the Committee's term of reference 2.3(d) which states that it is a function of the Committee "*to consult regularly with the Auditor General and any person holding an office of a like character*", and the provisions of the *Auditor General Act 2006*.
- 2.13 Subsequent to the Committee's referral, the Office of the Auditor General undertook an investigation. The Auditor General advised the Committee that he would report directly to the Parliament as his investigation identified a range of government and risk management issues that warranted reporting.

⁸ <http://www.parliament.wa.gov.au/web/newwebparl.nsf/iframewebpages/Committees+++Current> (current at 25 June 2008).

- 2.14 On 14 August 2007 the Committee advised the Council of this matter, including the fact that the Committee will not be tabling a report into the specific matters examined by the Auditor General.⁹
- 2.15 The Auditor General reported on the matter in his Fourth Public Sector Performance Report.¹⁰

Inquiry into the Memorandum of Understanding between Balga Senior High School and Manufacturing Industry Training Services Pty Ltd

- 2.16 On 28 June 2007 the Council referred an inquiry into the Memorandum of Understanding between Balga Senior High School and Manufacturing Industry Training Services Pty Ltd to the Committee. The reporting date for the inquiry was 18 October 2007. The Committee sought and was granted an extension of time to report to 29 May 2008.
- 2.17 Hon Peter Collier MLC was a substitute member for the inquiry for Hon Anthony Fels MLC and then for Hon Brian Ellis MLC.
- 2.18 Hon Brian Ellis MLC was a participating member for the inquiry.

Miscellaneous

Auditor General

- 2.19 The Committee held an informal briefing with the then Acting Auditor General on 9 May 2007. Issues discussed included changes arising from the *Auditor General Act 2006*, the work program of the Office of the Auditor General and the future working relationship between the Committee and the Auditor General.
- 2.20 The Committee received a briefing from the Auditor General on 18 June 2007 in relation to the Auditor General's report on the Office of Shared Services.

Iron ore industry

- 2.21 The Committee commenced consideration of whether to inquire into aspects of the iron ore industry in Western Australia in 2006.
- 2.22 The circumstances surrounding the Committee's initial considerations were the subject of the Select Committee of Privilege inquiry (see paragraphs 2.25 to 2.27).

⁹ *Special Report - "A Matter Arising from the 2006/07 Budget Estimates Hearings in Relation to the Western Australian Sports Centre Trust"*, Western Australia, Legislative Council, Parliamentary Debates (*Hansard*), 14 August 2007, pp3790-3791.

¹⁰ Auditor General's Report, *Fourth Public Sector Performance Report 2007*, Report 9, September 2007, pp24-29.

- 2.23 The Committee deferred its consideration of possible inquiry into this matter until the Select Committee of Privilege had reported. The Select Committee of Privilege reported on 13 November 2007. The Committee, however, did not reconsider this matter during this reporting period.

Commonwealth-State financial relations

- 2.24 The Committee commenced consideration of whether to inquire into Commonwealth-State financial relations in 2006. On consideration of the information obtained (attached at **Appendix 1**), the Committee resolved not to proceed with an inquiry into this matter during this reporting period. The Committee resolved to ask questions in relation to Commonwealth-State financial relations as part of its Ongoing Budget Estimates Hearings.

Special Report on a Matter of Privilege

- 2.25 In March 2007 the Committee tabled a special report on a matter of privilege in accordance with the Standing Orders of the Legislative Council which provides that any information involving an accusation against any Member (SO 422) and/or any possible breach of parliamentary privilege (SO 155) should be reported to the Council.
- 2.26 In this instance, the Chair of the Committee had been contacted by the Corruption and Crime Commission (CCC). It was alleged that there had been a breach of Committee deliberations, which the CCC were currently making inquiries about. The CCC had also asked for access to Committee documents, Members and staff.
- 2.27 Subsequent to this special report, the Legislative Council established the Select Committee of Privilege to inquire into the alleged breach of the Committee's deliberations.¹¹

Feedback on the form and content of annual reports

- 2.28 The Committee provided input into the joint review by the Department of the Premier and Cabinet and the Department of Treasury and Finance, of the requirements that agencies comply with in their annual reports.

Conferences

- 2.29 The Australasian Council of Public Accounts Committees (ACPAC) Annual Conference was held in Canberra, 11 - 13 April 2007. The theme of the conference was "Challenges Facing Contemporary Public Accounts Committees". The agenda is extracted below:

¹¹ For further information refer to: Western Australia, Legislative Council, Report, *Select Committee of Privilege on a Matter Arising in the Standing Committee on Estimates and Financial Operations*, November 2007.

- How public accounts committees (**PACs**), together with central agencies and Auditor Generals, can encourage better practice in contract management and risk management compliance with financial frameworks as responsibility is devolved to individual agencies
 - Different models for PACs in reviewing the work of auditors. How best to “add value” to the work of auditors
 - The role of PACs in safeguarding independence of Auditor Generals
 - The appropriate role of PACs in reviewing the work program of audit offices
 - Report on the Public Sector Governance and Accountability Research Centre/KPMG Study of PACs in Australia and New Zealand
 - The role of Auditor Generals in relation to outsourced government activities/functions
 - The importance of a Conceptual Framework for Public Sector Financial Reporting
 - The role of PACs in enhancing public sector reporting standards, including performance reporting in the public sector
 - Ensuring that PAC recommendations are implemented
 - Powers of PACs to set their own work program and the subsequent influence on their resources
 - How PACs deal with claims of public interest immunity by public sector agencies
 - The future direction of Public Sector Accounting Standards in Australia
 - Committee Activity Reports and Questions
 - ACPAC general business (ACPAC members only)
- 2.30 Representatives of committees from all Australian jurisdictions attended the conference (Members and staff) as well as representatives from overseas jurisdictions including New Zealand, Singapore and South Africa. Auditor Generals from Australia and overseas also attended.
- 2.31 Hon Giz Watson MLC presented a report on the activities of the Committee at the conference.

2.32 The Committee attended the conference as an associate member of the ACPAC. At the general meeting of the ACPAC the Committee was made a full member of the ACPAC.

2.33 Hon Giz Watson MLC, Lisa Peterson, Advisory Officer (General) and Renae Jewell, Committee Clerk travelled to Canberra to attend the conference. The total cost of travel for the Department of the Legislative Council was \$10, 006.

3 STATISTICS

Reports tabled

3.1 The Committee tabled five reports during this report period. These are listed in the table below.

Table 2

Report Title	Tabled Date
Special Report on a Matter of Privilege	20 March 2007
Annual Report 2006	29 May 2007
Budget Estimates 2006/07	16 August 2007
Interim Report on the Balga Works Inquiry: Request for a Member of the Legislative Assembly to Appear Before the Committee	18 September 2007
Annual Hearings in Relation to the Budget Estimates 2007/08	27 September 2007

Special reports tabled

3.2 The Committee tabled three special reports during this report period. These are listed in the table below.

Table 3

Report Title	Tabled Date
Substitution of Committee Meeting Day	8 May 2007
Special Report Advising of the 2007/08 Budget Estimates Hearings	10 May 2007
Special Report on a Matter Arising from the 2006/07 Budget Estimates Hearings in Relation to the Western Australian Sports Centre Trust	14 August 2007

Meetings and Hearings

3.3 The number of Committee meetings and hearings held by the Committee during 2007 is noted in the table below.

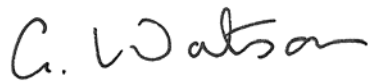
Table 4

Item	Number
Total number of meetings (including hearings)	45
Total number of hearings	50
Number of Hearings relating to the 2007/08 budget estimates	17

4 PLAN FOR 2008

4.1 In 2008 the Committee intends to:

- complete its consideration of the Budget Estimates for 2007/08;
- consider the Budget Estimates for 2008/09;
- complete its inquiry into the Memorandum of Understanding Between Balga Senior High School and Manufacturing Industry Training Services Pty Ltd; and
- address any other matters that arise which fall within the Committee's terms of reference.



Hon Giz Watson MLC
Chair

Date: 26 June 2008

APPENDIX 1
LETTER FROM THE
DEPARTMENT OF TREASURY AND FINANCE
DATED 30 JANUARY 2007

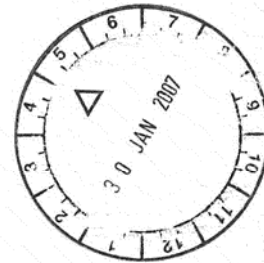
APPENDIX 1
LETTER FROM THE
DEPARTMENT OF TREASURY AND FINANCE
DATED 30 JANUARY 2007



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Our reference : 67068
6524513

Hon Giz Watson MLC
Chair
Legislative Council and Financial Operations
Committee
Parliament House
Harvest Terrace
PERTH WA 6000

Dear Ms Watson

COMMONWEALTH/STATE FINANCIAL RELATIONS

In response to the information requested in your letter of 8 January 2007 the Department of Treasury and Finance has prepared the attached advice.

I trust this will be of assistance.

Yours sincerely

MICHAEL MEGAW
CHIEF OF STAFF
OFFICE OF THE TREASURER

Enc.

30 JAN 2007

DEPARTMENT OF TREASURY AND FINANCE
BRIEFING NOTE

COMMONWEALTH/STATE FINANCIAL RELATIONS

- (i) *A list of the areas that are experiencing a cost shifting between the Commonwealth and the State and details of the cost shift.*

At the broadest level, cost shifting from the Commonwealth to the States is reflected in declining Commonwealth grants to the States (collectively) as a proportion of Commonwealth taxes, over the past two decades. Commonwealth grants to the States over the period 1981-82 to 1985-86 averaged 31.6% of Commonwealth taxes, falling to 24.9% of Commonwealth taxes over the period 2001-02 to 2005-06. Alternatively, as a share of GDP Commonwealth grants to the States over the period 1981-82 to 1985-86 averaged 7.2%, falling to 6.2% over the period 2001-02 to 2005-06. This has forced the States to turn to their narrower, less economically and socially desirable tax bases (e.g. by liberalising gambling activity in some cases) to fund increasing expenditure pressures.

For some years (1985-86, 1987-88, 1991-92 to 1993-94), the Commonwealth indexed financial assistance grants to the States (now replaced by GST grants) by only an inflation factor (i.e. with no provision for population or real economic growth). At various stages (1988-89 to 1990-91, 1996-97 to 1998-99) it even reduced grants in real terms, or withheld grants specifically to help balance its own budget.

The reduction in grants to the States as a proportion of Commonwealth taxes would have been even larger if the replacement of some of the States' less desirable taxes (e.g. financial transaction taxes) by the GST had not resulted in a one-off increase in grants to the States.

Some more recent examples of this kind of Commonwealth cost shifting include:

- the Commonwealth unilaterally changing part of the formula for calculating the top-up grants required to ensure that the States were not financially worse off in the early period of the GST funding arrangements (\$20 million cost to Western Australia);
- the Commonwealth discontinuing National Competition Policy (NCP) payments after 2005-06 (around \$70-80 million annual cost to Western Australia); and

- 2 -

- the Commonwealth providing inadequate funding escalation for increasing hospital cost and demand pressures, while requiring States to provide universal eligibility for free hospital services (this funding shortfall for Western Australia is estimated to be growing at about \$25 million per annum).
 - Although difficult to quantify, the interface between the Commonwealth and State responsibilities for health is particularly prone to cost shifting. The shortage of doctors in remote areas has led patients with primary care needs to attend public hospital emergency departments instead of GP clinics (with costs funded by the State instead of through the Medicare system) and inadequate Commonwealth funding of nursing homes has led to inefficient occupation of beds in public hospitals by nursing home-type patients.

Another form of Commonwealth cost shifting to the States has occurred through the Commonwealth's imposition of conditions on grants to the States to achieve Commonwealth policy objectives through State programs. Over time, specific purpose payments (SPPs) as a share of total Commonwealth grants have risen substantially (from 24.0% in 1965-66 to 41.0% in 2005-06). At the same time, conditions on SPPs have become increasingly prescriptive.

In this regard, matching conditions that prescribe how much a State must spend from its own sources on a partly SPP-funded service have become the norm, often with no regard for differences between States in pre-existing 'effort', or the appropriateness of the spending.

- The National Action Plan on Salinity and Water Quality is a significant recent example in Western Australia. The State was required to match new funding contributed by the Commonwealth with new money of its own, despite its substantial existing programs in this area. The State was also required to allocate funding to a large number of local projects on an 'equitable' basis rather than being able to concentrate funding on projects that independent experts had indicated would deliver the greatest public benefits.
- The Commonwealth requirement to maintain real terms spending on vocational education and training has prevented the State from applying Government-wide efficiency dividends or savings initiatives to this sector.

Some SPP agreements now effectively prescribe how (and when) services are to be delivered or how the programmes or projects are to be managed (including in an industrial relations context), in addition to requiring Commonwealth Government as well as State Government approval of individual projects under the SPP program.

SPPs can have a significant negative impact on State Government budget flexibility. Where the conditions do not demonstrably address national interest objectives and are inconsistent with State priorities, the result may be reduced service delivery outcomes, higher State taxes and a misallocation of resources.

(ii) A list of the names of the Intergovernmental Agreements currently in effect that have financial implications on the State.

Intergovernmental Agreements that have financial implications include the following.

- The 1999 Intergovernmental Agreement of the Reform of Commonwealth-State Financial Relations (the GST agreement).
- Agreements underpinning the 1995 National Competition Policy (NCP), namely the Competition Principles Agreement; the Conduct Code Agreement; and the Agreement to Implement the National Competition Policy and Related Reforms (Implementation Agreement).
- The 2006 Intergovernmental Agreement on a National Water Initiative.
- SPP agreements (e.g. the Australian Health Care Agreement), which generally include multilateral and/or bilateral agreements. A list of these payments is available from Appendix B of Commonwealth Budget Paper No.3 (Federal Financial Relations).

(iii) A history of the share of funding provided by the Commonwealth compared to the share of funding provided by the State in the areas to which the Intergovernmental Agreements referred to in (ii) relate.

The Department of Treasury and Finance does not typically keep a record of this type of information.

Over time, through the use of SPPs, the Commonwealth has increased its share of funding for specific State-provided services in a number of areas, including education and health since the early 1970s. However, the Commonwealth's share of funding for State services through SPPs in recent years has declined (SPPs comprised 13.9% of Western Australian State revenues in 1999-2000, compared with 12.6% of State revenues in 2005-06).

As the introduction of the GST has been accompanied by abolition of State taxes, the Western Australia's dependence on Commonwealth grants has increased from 40.0% in 1999-2000 to 44.8% in 2005-06.

- 4 -

As noted, SPP agreements have increasingly included matching funding arrangements where the Commonwealth and State contribute an agreed proportion of the proposed funding. While comprehensive data is lacking, we consider that in recent years the State share of funding under these agreements has tended to grow faster than the Commonwealth. This is largely because Commonwealth indexation arrangements in these agreements are generally inadequate and the States are left to meet the burden of cost/demand pressures, particularly in the health sector.

Furthermore, in a couple of recently negotiated agreements the matching arrangements have been varied to the States' detriment - the States' relative contribution was increased from 40/60 to 50/50 in the latest Supported Accommodation Assistance Program agreement, and States were required to commit significant increases in funding for the last Disability Agreement

While Western Australia is, in these above respects, in a similar position to other States, there are issues that are more specific to Western Australia.

Western Australia presently receives about a population share (10%) of total Commonwealth grant funding. However, our share of GST funding is forecast to decline sharply over the next few years (from 10% in 2006-07 to 8.6% in 2009-10), particularly reflecting the impact of the recent high growth in the State's property market related revenue and mining royalties. (Under the Commonwealth Grants Commission's equalisation methods for distributing GST grants among the States, if a State has stronger than average growth in revenue capacity, there is an offsetting redistribution of GST grants away from that State to the other States.)

Meanwhile, Western Australia's net contribution to the Commonwealth budget (i.e. the extent to which Commonwealth taxes and other revenues sourced from Western Australia exceed Commonwealth spending for Western Australia) is soaring. The State's net contribution rose from an estimated \$3.2 billion in 2003-04 to \$4.1 billion in 2004-05 (see the Federal Affairs Chapter of State Budget Paper No.3 for details), and is projected to rise further, reflecting the strength of the Western Australian economy.

While a positive contribution to the Commonwealth budget is to be expected, it is considered that the Commonwealth has inadequately recognised the State's needs and has underspent in Western Australia (eg. on health in remote areas, Aboriginal communities, telecommunications and infrastructure) and overtaxed in Western Australia (eg. allowing insufficient tax deductions for the cost of living in remote areas, and for depreciation of equipment). This may be a consequence of Western Australia's remoteness from the seat of national government power and its relatively small population (and hence influence), together with its unique geography and economy.

The Department of Treasury and Finance *Discussion Paper on Commonwealth-State Relations: An Economic and Financial Assessment of How Western Australia Fares* (see copy attached) provides further detail on these issues. A couple of specific examples are:

- the State receives only 11% of Auslink funding, despite having 22% of the national road transport network and contributing 30% of the nation's merchandise exports; and
- the Commonwealth receives the majority of the fiscal returns from Western Australia's major resource projects through its broad revenue bases - especially Petroleum Resource Rent Tax, personal income tax and company tax. In addition, a large proportion of the State's share of fiscal benefits tends to be redistributed to the other States by the Commonwealth Grants Commission process. Yet the Commonwealth Government makes very little contribution to the infrastructure and other costs of supporting such developments.

Particularly to the extent that Western Australia has much of its economic potential still to be realised, failure to recognise the State's needs in a way that holds back its further development is likely to be to the detriment of national economic and welfare outcomes.

DEPARTMENT OF TREASURY AND FINANCE

29 January 2007