# GST carve up “one of the worst policy decisions” of the past 20 years

By **Contributor** - April 8, 2022

*It’s scandalous the federal government will be adding almost $20b to its deficit in order to hand over the equivalent amount to WA, the only government in Australia running a surplus, says economist Saul Eslake.*

## Opinion

**By Saul Eslake**

THE cost of one of the worst policy decisions of the past 20 years – the changes to the way GST revenues are carved up among the states – continues to escalate.

It’s just scandalous that the federal government will be adding almost $20b to its deficit in order to hand over the equivalent amount to WA, the only government in Australia running a surplus.

I certainly hope that the way in which the GST revenue is ‘carved up’ will change as a result of the review which the Productivity Commission is scheduled to undertake in 2026 – and preferably back to the arrangements which had served Australia perfectly well until they were changed as a result of the ‘deal’ imposed on the states and territories by the current federal government in 2018.

But whether that happens will depend importantly on (a) the terms of reference for the PC’s enquiry, and (b) who from the PC conducts it, and how they conduct it.

The terms of reference for the PC inquiry which led to the changes imposed in 2018 were deliberately written in such a way as to almost guarantee that the PC would recommend the sort of changes that WA wanted (a classic example of the advice which Sir Humphrey Appleby used to give to Prime Minister Jim Hacker in the BBC TV 'sitcom' Yes Prime Minister, "never call an enquiry until you know what it is going to say").

And that PC enquiry was conducted in a very un-PC like way, with scant regard for the evidence, and with what staffers who worked on that inquiry have since told me was a "pre-determined conclusion" in mind.

That's why I have argued that the enquiry should be brought forward to, say, 2023; that other states and territories (not just WA) should have a say in the terms of reference for the enquiry; and that they should also have some say in who conducts the inquiry.

In response to those who think there was something "unfair" about the way in which GST revenues were distributed prior to the current changes coming into effect (or the way in which they might have been distributed had those changes not been imposed) several things.

First, most Western Australians appear not to be aware that the principles which the Grants Commission has used to determine how 'untied grants' from the federal government to states and territories since 1936 – ie, that citizens of every state (and more recently territory) should be able to have provided to them the same standard of public services (schools, hospitals, policing, child protection, social housing etc) as in other states, without having to face significantly different burdens of state taxation – were first devised in response to WA's legitimate grievances about the way that the federation had worked between 1901 and 1933, when Western Australians voted 2-to-1 in favour of seceding from the Commonwealth (something which the Privy Council in London subsequently ruled was not possible).

And the application of those principles meant that, for 70 years afterwards, WA got a larger share of whatever 'untied' federal grants were going around (in the form of 'tax sharing grants in the years after the Commonwealth took over income tax in 1942, 'financial assistance grants', and after 2000 the revenue from the GST) than it would have obtained from an 'equal per capita' distribution of that money – in recognition of the fact that it was expensive to provide state-type public services to a population thinly spread across a huge area, at a time when commodity prices were relatively low, and WA didn't have much capacity to raise revenue from its own resources.

Second, beginning in the early 2000s, WA's fortunes were transformed – not through any great effort on WA's part (apart from a few people like Gina Reinhart and 'Twiggy' Forrest) – as a result of China's enormous appetite for the minerals and energy resources with which WA just happened to be so richly endowed, and its (China's) willingness to pay hitherto undreamt of prices for those resources (thereby also forcing existing purchasers of those resources, such as Japan and Korea, to pay the same sky-high prices for those resources).

Again, I stress that this was more a matter of 'good luck' than 'good management'.

Most of the capital required to develop those mines came from shareholders located in the eastern states or in foreign countries: and a lot of the workers came from the east or overseas as well.

I think most Western Australians don't realize just how much richer they have become than the rest of Australia – WA's per capita gross product (a good proxy for WA's ability to raise revenue from its own sources) has been more than 40 per cent – yes, 40 per cent! – above the national average.

That is a much bigger margin than NSW or Victoria ever were richer than the rest of Australia.

So the "unprecedently low" share which WA was getting of GST revenue (relative to a notional 'equal per capita' share – although to re-iterate, federal grants to states and territories have never been distributed on an equal per capita basis) was only "unprecedented" because there was no precedent in Australian history for one state being so much richer than the rest of Australia, as WA has become in the past twenty years.

In that sense, WA's complaints about the way in which the GST revenue sharing system had been operating are similar to those sometimes heard from very rich people to the effect that they have "earned" their high income or wealth, and that there is something "unfair" about them paying a higher proportion of their income in tax than most of the rest of the population.

Or, as I have often said in Perth (as well as over on this side of the country), given that WA was a beneficiary of the pre-2018 system for about seven decades, Western Australia often sounds like a pensioner who has won the lottery, and then complains about losing the pension and having to pay income tax.

Former WA treasurer Christian Porter was largely responsible for the financial mess WA temporarily found itself in (after he had scarpered off to Canberra): he prepared his budgets on the explicit assumption that successive federal governments would "fix" the GST revenue sharing arrangements (in the way that WA had been demanding) and so went on spending as if extra GST revenue would be forthcoming – which of course it wasn't.

### Box 5.1 **Western Australia's budget position**

After 10 years of strong growth, Western Australia's royalty revenue peaked in 2013-14 and declined substantially thereafter. Due to the three-year assessment period and two-year lag, Western Australia's GST payments have remained heavily influenced by previously high royalty revenues, contributing to pressure on the State's budget. The WA Government argued that in this instance fiscal equalisation exacerbated the effect of the downturn on the State's finances.

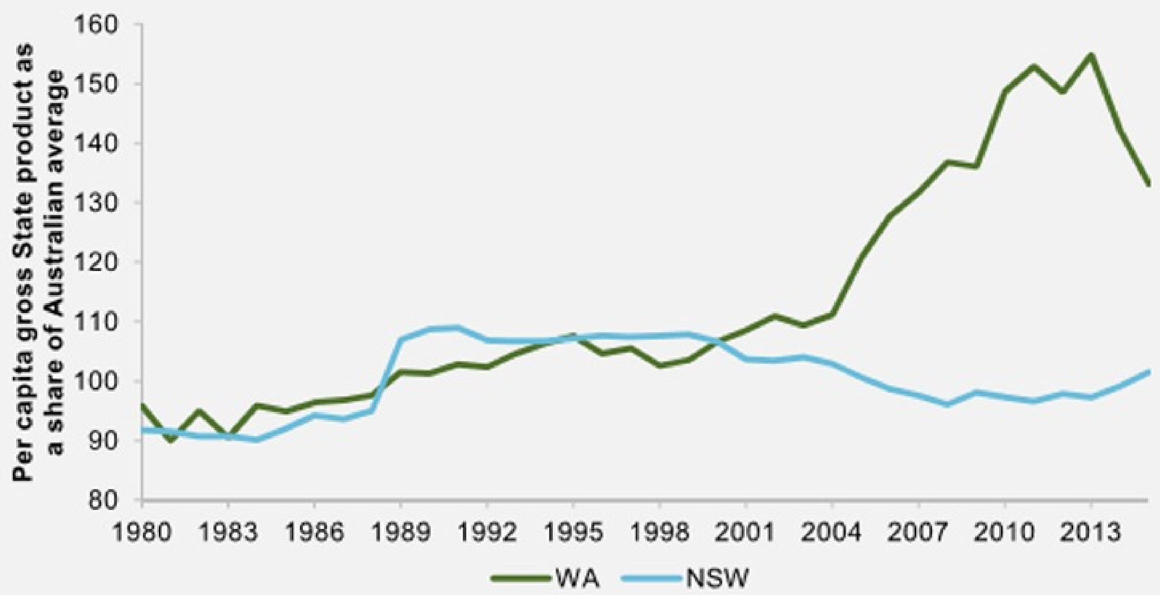
Western Australia's falling GST shares were nonetheless predicted. For example, in its 2011-12 budget, the State projected a fall in its relativity from 0.72 to 0.33 by 2014-15 — its actual relativity in 2014-15 was 0.38 (WA Government 2011a). In later years, however, the WA Government based its spending decisions on the assumption that a 0.75 floor would be introduced. The State Treasurer noted in his budget speech:

> What we reasonably anticipate is that in 2013-14 the CGC will have brought in a new GST system. We expect it will produce a floor of around 75 per cent of our population share of the GST. Therefore we expect revenue of $1.8 billion in 2013-14 and $2.5 billion in 2014-15. These amounts will allow for reduced borrowings and will be used to progressively reduce existing debt to less than $18 billion while maintaining strong infrastructure spending. (Porter 2011, p. 3)

Many have attributed Western Australia's current fiscal position to continued high spending, despite falling GST shares. Eslake (2017b), for example, argued:

> Despite the sharp decline in its share of GST revenues, the WA government's total revenue per head of population in 2015-16 was just A$67 (or 0.7%) below the average for all states and territories. By contrast, by 2015-16 the WA government was spending over A$1000 (or 10.5%) more per head of population on 'operating expenses', than the average of all states and territories …
>
> WA's present fiscal woes are the result not of a flawed system of distributing revenue from the GST among the states and territories, but rather of its inability to control its own spending.

Moreover, Eslake (2017a) has noted that while the level of Western Australia's relativity is unprecedented, so is its relative growth in per capita gross state product (see chart below).




While Western Australia is currently receiving less than it would under fully contemporaneous equalisation, it received more while mining royalties were increasing. The CGC has estimated that from 2010-11 to 2015-16 growth in iron ore royalties resulted in Western Australia retaining about $7 billion more than it would have under fully contemporaneous GST payments (CGC 2015d).

**Saul Eslake is one of Australia's best-known economists**