

## REVIEW OF FINANCIAL ASSISTANCE GRANTS

### ARRANGEMENTS

MR. GORTON - I shall read a statement which has been prepared for me and which I believe is to be circulated. The main purpose of this meeting is to further discuss the new general revenue grants arrangements between the Commonwealth and the States to apply from the beginning of 1970-71. These arrangements embrace both the method of determining the annual general revenue assistance to each State, and the forms of such assistance, and they are therefore of very great importance in determining the future pattern of Commonwealth-State financial relationships.

Dealing with the particular question of general revenue grants, at our meeting in February I expressed a willingness on behalf of the Commonwealth Government to discuss matters relating to the financial assistance grants and to look, as you had suggested, at the base total and to look, as you also suggested, at such aspects as the betterment factor. I also expressed a willingness to discuss and seek to ameliorate one of the problems of the States which has been frequently put forward; that is, the difficulty which you have seen arising as a result of some of the loan money which the States secure being provided, in fact, from revenue gathered by the Commonwealth rather than by money borrowed from lenders in the normal way. In the intervening months we have had discussions between our Treasury officials, that is of the Commonwealth and the various States, and I think these discussions have been helpful to both of us.

Today it is my purpose and my responsibility on behalf of the Commonwealth Government to put before you proposals for the ensuing five years commencing on 1st July next. In offering assistance specifically directed at helping the States to meet interest and sinking fund charges on the State debt we have had in mind the concern which Premiers have expressed at the annual growth of State debt and particularly at the rate this debt has been growing in relation to the rate of growth of Commonwealth debt. We have also taken into account our undertaking to bear in mind, during our present review, the question of offsetting any additional financial burden on the States which might arise from the Commonwealth's decision in 1968 to remove the income tax rebate on Commonwealth loan interest.

In the Commonwealth's consideration of these proposals, we have aimed at providing an average annual rate of increase in total Commonwealth revenue assistance to the States substantially above the increases that would have been produced if the present grants arrangements continued unaltered. For example, if - on the basis of past trends in increases in average wages and population - the present grants formula would have resulted in the grants growing at an average of 9.9% each year over the next five years, we have calculated that the overall effect of the Commonwealth's new proposals would be to increase that average rate of growth to at least 12.5% per year.

I turn now to outline in broad terms what we have in mind for each of the four sections of the Commonwealth proposals. Later I shall circulate proposals setting out their essential features. On the question of taking over State debt and of interest-free capital grants, we propose that the capital grant begin at \$200m in 1970-71 - this is the sum of money which we propose to make available as a grant rather than, as has happened in the past, as a loan - and that it should thereafter increase at the same rate as the total works and housing programmes. The States' formal Loan Council borrowing programmes will be lower each year by an amount equal to the capital grant, of course, and the payment of the grant by the Commonwealth will be conditional on agreement being reached on the size of the total borrowing programme. As the primary purpose of the grant will be to relieve the burden of debt charges on non-revenue producing capital expenditure, it will be designed to help finance expenditure on capital works and services from which debt charges are not recouped, such as schools, police buildings and the like. However, while we would appreciate from you an informal assurance that the funds will be used in this way - that is, for non-recoupable purposes - there will be no specific or legal conditions attached to the expenditure of the grant.

As the grant will not form part of the States' borrowing programmes, its distribution between the States will not be a matter for legal determination by the Loan Council. While it will therefore probably devolve on the Commonwealth to accept final responsibility for determining the distribution of the total grant each year between the States, we are hoping that it will be possible to agree to the distribution with you beforehand and in a co-operative way.

It is not possible to estimate precisely the debt charges savings to the States that will result from this proposal in the year each grant is made, although in future years the saving will obviously be a full year's interest and sinking fund. The savings in the first year will depend on the timing of loan raisings during the year, and the overall savings will depend, among other things, on the size of the States' borrowing programmes in the future, on trends in interest rates and so on. However, on the basis of recent trends in increases in loan programmes and of present interest rate patterns, we estimate that over the 5 years 1970-71 to 1974-75 the total debt charges savings to the States from this annual grant will be of the order of \$148m, which is additional to some small saving in 1970-71 which we have not included in the tables which will be circulated subsequently. In other words, we are saying that there will be a saving to the States from this in the first year but it is difficult to estimate how much that saving will be.

It may only be as much as \$1 million. We are therefore discounting it, not counting it in as assistance to the States, and saying that it is in the second year of this programme that the States will receive the full benefit of this \$200 million, because they will not be paying interest and sinking fund on \$200 which they would otherwise be paying interest and sinking fund on, and that will be the basis of our calculations on this.

On the question of the taking over of existing State debt, I understand that officers have agreed that for a number of reasons it would be impracticable for State debt to be taken over by the Commonwealth before June 1975 except in a notional sense. That does not matter because it is proposed that from 1970-71 to 1974-75 the Commonwealth will reimburse the States by way of section 96 grants for the interest and sinking fund charges on a progressively increasing amount of State debt. So that although the debts are not actually taken over, the cost of the debts to the States is taken over. Specifically, we propose that \$200 million of State debt be taken over, in the sense just explained, at the beginning of each of the next 5 years so that by the commencement of 1974-75 the Commonwealth will be meeting the debt charges on a full \$1,000 of State debt. The arrangements for the formal transfer of the debt from the States to the Commonwealth in June 1975 will be a matter to be settled later.

I understand that Commonwealth and State officials agreed an appropriate parcel of \$1,000m of State debt - that is after going through the various debts which were outstanding - the officers agreed that a debt maturing at such and such a date and at such and such an interest rate, and then another debt, would make up the parcel which would be taken over. They agreed on a parcel of \$1,000m of State debt carrying an average interest rate of 5.5%, which is significantly higher than the average interest rate of around 5% on all existing State debt. I do not propose to go through the precise arrangements here, but the Commonwealth accepts the conclusions reached by the committee of officials appointed to examine possible procedures and, with the additional arrangements I have already outlined, we propose to proceed along the lines recommended by the officials. The arrangements are summarised in the document . shall be circulating to you.

The grants, which will cover the average interest charges of 5.5% together with the annual sinking fund contributions of .25% on the debt taken over, will be \$11.5m in 1970-71, \$23m in 1971-72, \$34.5m in 1972-73 and so on, giving a total of \$172.5m available to the States over the next five years. I point out that there has been some discussion as to the method of taking over this \$200m of debt. It had been suggested that perhaps in the first year we would take over half of it, say, in September and the other half in March, and only from those debts would we reimburse the States for the interest and

sinking fund the Commonwealth had to pay. But after discussion, we believe that when we as a Commonwealth said we would take over \$200M of State debts each year it would be accepted by the States that we would take over that \$200M at the beginning of the year and pay the interest and sinking fund at that date for that year, and this is what we propose to do.

It is the Commonwealth's view that the distribution between the States of the debt notionally taken over (and hence the distribution of the grants to meet the debt charges) should be in proportion to total outstanding debt under the Financial Agreement as at 30 June 1970.

As I have mentioned, the two proposals on debt should substantially reduce the rate of growth of debt charges over the next 5 years. The actual saving in debt charges as a result of the two debt proposals - that means the actual additional resources available to the States as a result of the two debt proposals, is estimated as follows: \$11.5 M in 1970-71, \$37M in 1971-72, \$63.3M in 1972-73, \$90.4M in 1973-74 and \$118.3M in 1974-75, giving a total of \$320.5M over the quinquennium. This is the amount that these two proposals will add to the resources of the States, subtract from the resources of the Commonwealth and inject into the spending capacity of the economy. In addition to this substantial assistance for debt charges, we propose a decided improvement in both the amount and the rate of growth of the financial assistance grants themselves. We suggest

that for 1970-71 the formula grants paid to each State will be determined by applying the present formula to the formula grants paid to each State in 1969-70, that is by applying the present betterment factor to the grants received by each State in 1969-70, which I believe would add \$100m to the amount available to the States this year, with the continuing addition in the case of Queensland of \$2m to the 1969-70 base but, of course, not including any special assistance approved last February or other adjustments made since then. In addition, a further amount will be distributed between the States in the same proportions as their new 1970-71 formula grants, and this amount will then be included in the base for determining the formula grants for 1971-72.

For purposes of determining the formula grants after 1970-71 we are proposing to improve the grants formula by improving the betterment factor from its present 1.2% per annum to 1.8% per annum, an increase of 50% in the size of this element of the grants formula.

Taken together we envisage these improvements, excluding the debt assistance and grants in lieu of loan which I have already mentioned, on the basis of present estimates of increases in average wages and population will mean that the total financial assistance grants - excluding the ones I have mentioned - should be some \$384m higher in this forthcoming quinquennium than they would have been under the existing formula.

We have given very careful consideration to the position of Queensland and have come to the conclusion that in spite of the considerable improvement that has been effected in its share of the grants over the last 5 years, the grants being received by that State are still too low relative to the other States.



We therefore propose to continue the arrangements existing during the present quinquennium of adding \$2m each year to the base on which Queensland's grant is calculated.

Other States have also requested an improvement in their share of the grants, mainly based on arguments about per capita relativities. We have not been sufficiently persuaded by such comparisons and we are not prepared at the present time to suggest any special action to adjust the shares of States other than Queensland, except for what I shall now say about Western Australia.

An additional grant of \$15.5m was paid to Western Australia in 1968-69 and 1969-70 in lieu of the grant it had previously been receiving on the recommendation of the Commonwealth Grants Commission. When the State withdrew from the Commonwealth Grants Commission in 1968, it was agreed around this table that the sum of the State's 1969-70 financial assistance grant and the \$15.5m would form the base of consideration for purposes of the present review. Since 1968-69 Western Australia has been receiving increases in its base grant and they have been escalated, but the \$15.5m has not been incorporated in the base grant and has not been subject to escalation but has been merely paid from the Commonwealth revenue in lieu of the Commonwealth payout through the Grants Commission.

I am sure that it will be appreciated that there could be no prior commitment by the Commonwealth to continue to pay any particular amount to a State. We have noted that since 1967-68 there appears to have been a significant improvement in the relative capacity of Western Australia to finance its Budget expenditure at a standard at least comparable with that of other States. This means that, if the State continued to receive its present share of the revenue grants, including the special amount of \$15.5m, the situation would become increasingly unfair to the other States and could result in a significant distortion in the allocation of governmental funds between the States.

We are aware, of course, that the rapid rate of population growth and economic development in Western Australia has brought considerable problems, particularly on the capital side, and we are therefore prepared to give sympathetic consideration to that matter. The question of any special increase in shares of the Loan Council borrowing programmes is, of course, a matter for the Loan Council to decide. I make it clear, however, that the Commonwealth, subject to agreement on other matters, will support in the Loan Council a special increase of \$3m in the State's 1970-71 borrowing programme for larger authorities.

It is not possible to estimate accurately the effect that the proposals I have outlined will have on

the total revenue assistance provided to the States over the next 5 years. The actual amounts and rates of increase in total revenue assistance each year will depend, amongst other things, on the rate of increase in average wages and in population. However, on the assumption that these are much the same over the next 5 years as they have been over the 5 years of the present grants arrangements, total revenue assistance will be approximately \$54m more in 1970-71 and over \$700m more over the next 5 years, than if the present grants arrangements had continued unaltered. These are, of course, very substantial additions indeed. Let me point out that when one says \$54m more one means \$54m more than the \$100m more that the existing formula will provide.

As is well known, the distribution of the financial assistance grants is weighted in favour of the 4 less populous States in that their grants, in per capita terms, are higher than those of New South Wales and Victoria. In addition, Tasmania receives an annual special grant on the recommendation of the Commonwealth Grants Commission while Western Australia has recently been receiving an additional grant in lieu of the special grant which it previously had.

The general principle underlying the distribution of the general revenue grants is that each State should be enabled to provide government services of a standard broadly comparable with those of each other State without imposing higher taxation or other charges. However,

the principle is rather easier to state in general terms than it is to apply in practice and there are many problems both of a practical and conceptual nature which arise in attempting to determine the correct distribution of the grants. While we believe that the present distribution of the grants is a fair one, we do not believe that it is necessarily correct in precise terms. With the grants being so large an element in the State's finances, we think that it is of considerable importance that the distribution should come as close as possible to achieving the general objective I have just stated.

But there are many difficulties in attempting to determine the correct distribution. These difficulties, if anything, have become more significant as a result of the very rapid changes recently occurring in the finances of some States. We encountered some of these difficulties in the course of the present arrangements when we examined the requests made to us by individual States. I strongly feel that it would be desirable to have independent investigation and advice on this question for the purposes of the next review of the arrangements. I believe that if the Premiers were disposed to accept this the best approach might be for the Commonwealth Grants Commission to be given this task.

As the Premiers know, the Commission has in the past been responsible for recommending annual grants to the three less populous States, but only Tasmania now

remains a claimant State. Whether it continues to do so or not will be a matter for it to decide. But in any case the Commission could be given the task of recommending on the distribution of the grants between all the States, not necessarily annually but mainly for the purposes of the regular reviews of the revenue grants arrangements. But the success of any scheme along these lines would obviously depend on full co-operation being given by the States. I therefore ask the Premiers to consider that suggestion and at a later stage to let us have their opinions.

We would also be prepared to consider the possibility of giving the Commission the task of examining the share of the grants paid to a particular State between reviews of the grants arrangements. For example, Western Australia may wish to put a case before the Commission as to the appropriateness of its proposed share of the grants. If we were to implement these proposals there would, of course, be a number of matters to decide as to the way the Commission would work and we would obviously have to give close thought to them. As I say, I would welcome the views of the Premiers on this whole question.

I think that the proposals outlined constitute a significant contribution towards an improvement in Commonwealth-State financial relationships. It will be said, no doubt, that they will not solve all the financial problems with which the States are faced. We, for our part, well appreciate the continuing pressure on governments to improve the standard and range of services provided by governments. But we have got to have regard to the limitations imposed by the supply of real resources. In recent years expenditure at

all levels of government has been increasing at a significantly faster rate than gross national product, and the total of Commonwealth revenue assistance proposed should ensure the States of a source of revenue that will grow significantly faster than the gross national product. However, progress must necessarily be achieved in stages and we must have regard to the need to provide scope for the growth of the private sector of the economy. If we are to provide such a substantial increase in revenue assistance and in resources available to the States it should be on the basis that there are no significant changes in the financial relationships between the Commonwealth and the States during the period of the agreement. In particular, we would expect that the States and their authorities will continue to pay pay roll tax and that the distribution of tax resources between the Commonwealth and the States will remain unchanged.

We are aware, of course, that it has been one of the States' main arguments that they should share in the natural growth of revenue on income tax and while I do not accept that there should be any fixed relationship between income tax collections and the revenue grants - any fixed relationship between the growth of income tax revenue and the growth of revenue grants - I would mention that we expect the growth of revenue assistance under the proposals outlined to be close to, if not in excess of the rate of growth in the total of income tax collections from individuals and companies at the presently prescribed rates.

Well, gentlemen, those are the matters which I see as our having to discuss: First, a taking over of \$200m of State debt each year at the beginning of the year and the paying of interest and sinking fund on it; secondly, the provision each year of \$200m of grant which would otherwise have been loan; thirdly, the question of what additions should be made to the base grants for 1970-71, and what new betterment factor should be used to escalate this over the 5 years coming.

I hope that some tables on these matters have been circulated to the Premiers. It is possible that the Premiers may wish now to examine them during an adjournment.

MR ASKIN - Yes, that is the situation as far as I am concerned and I think the other Premiers feel as I do. As you know we submitted our case in writing last February and I still think that what we suggested then is the best way to preserve the federal system. You put up alternative proposals and they are quite involved. I would like to say quite a lot about the adequacy of some of the amounts under the different sub-headings - or rather, as I see it, the lack of adequacy. However, I think that should wait until we have had a talk amongst ourselves. Most Premiers would probably want to have a talk with their advisers first and then we will get together as a team to discuss what is involved and the implications of the proposals you have just put. It may be some time before we are ready to meet again, because there is quite a lot of meat in these various proposals. At this stage I can only say that I hope we will be able to prevail upon you to do a bit better than you have already set out, but to do that I know we must come back with some cogent arguments. I am sure you will understand that I have just made a few brief remarks and that I will want to speak at length on the base grant, betterment factor and so on. I do not think that this is the appropriate moment to do that and, subject to the concurrence of my colleagues, I suggest we adjourn so that we may talk separately first and then together.

SIR HENRY BOLTE - Should we go into Loan Council now?

MR. GORTON - It is up to the meeting. I thought the Premiers might like to examine these proposals first in Premiers Conference, come back and make a few more comments on them before we go into Loan Council. The Premiers will have to move out of this room to study the proposals.

MR. ASKIN - I think Loan Council to some extent depends on a study of the first proposals. I would like to get these cleared up one way or the other. I recognise the importance of Sir Henry's suggestion, but Loan Council will depend closely on matters decided here. I think we should try to dispose of these matters first. Would it be possible for us to have a copy of your statement?

MR. GORTON - I would hope so. This time it was written out beforehand. It will get to you as soon as possible. Mr. Bjelke-Petersen, do you agree?

MR. BJELKE-PETERSEN - Yes. I think we ought to get together ourselves first. This is fairly involved Mr. Gorton.

MR. GORTON - That is what we will do, and I will be at your command when you are ready. Could I just say



that I understand what the Premier of New South Wales has said about adequacy. However, on two of the matters that are before us I thought there was virtually complete agreement. The first of those is the taking over of \$200M of State debt. I thought the officers had agreed on that. I thought you would be pleased that we had decided to take over the interest and sinking fund charges as from the beginning of the year. I thought we had agreed on the \$200M a year grant, which otherwise would be a special loan. I do not know how the Premiers feel, but I do not anticipate much discussion on those two points.

MR ASKIN - I think the main discussion will centre on the first two items of the 5-point proposal you made last February - that is, the base grant and the improvement, which you said at the time would be adequately improved, and the betterment factor.

MR GORTON - That is what I thought, too.

MR ASKIN - These will occupy most of our time.

SIR HENRY BOLTE - Except that there could be a formula used to decide how to apply these other proposals.

MR GORTON - There will be discussion clearly on whether the distribution should be as we have suggested - it is only a suggestion - on the question of taking over State debt and whether that will be distributed in proportion to the total debt of the States.

SIR HENRY BOLTE - Or would be in proportion to the recoup percentage of the States?

MR GORTON - That I am sure will be the subject of discussion amongst the Premiers, but the total amount is agreed. The payment of interest and sinking fund charges is agreed. I shall listen with great interest to how various Premiers think it should be distributed, but the total will be the same. Then we shall adjourn now until the ringing of the bells.

The Conference adjourned