**HON. RICHARD COURT, AC**

29 November 2013

Submission to the National Commission of Audit

## Correcting Vertical Fiscal Imbalance – A Simple, Practical Proposal

Commissioners

Ever since our Federation commenced there has been an ongoing issue as to how the States can fund the extensive delivery of services for which they have Constitutional responsibility as more and more of the nation's revenue streams flow directly to the Central Government.

The major stumbling block in the State's finally reaching agreement for a Federation was in relation to fair revenue sharing arrangements and to assist in getting the proposals across the line there was a Braddon Clause included which guaranteed the State's access to a strong revenue source (sharing of the surplus Customs revenues) for the first decade remembering at the time of Federation approximately three quarters of colonial revenues came from Customs and Excise duties.

The Braddon Clause required the Commonwealth to restrict its spending to no more than 25% of the Customs and Excise revenues so that at least 75% of the net surplus must be distributed to the States. The Braddon Clause was never extended.

Since Federation we have seen countless interpretations of the Commonwealth Constitution by the High Court giving the Commonwealth Parliament's legislative powers wider rather than narrower scope and meaning.

Following a succession referendum in Western Australia on the 8 April 1933 supported with a 2:1 majority the Commonwealth responded to this protest by the establishment of the Commonwealth Grants Commission to assist into a fairer distribution of revenues between the States.

During the Second World War we then saw the Central Government "temporarily" take over Income taxing powers, but when peace returned the States Income Tax did not.

We did see the Central Government introduce the Payroll Tax which was then transferred to the States in 1971.

When the High Court made a decision which ruled that the States could not raise licence fees for wholesalers licences covering areas like tobacco and alcohol the Federal Government needed to step in to collect these taxes on behalf of the State.

In many ways this was the catalyst in 1998 when the Howard Government introduced legislation for the GST.

When the GST was introduced there were projections made as to what the collections and distributions would be between the States at the same time there were projections for the Federal Governments collection of Income Tax and Company Tax.

The GST was providing a growth revenue source at a greater rate than originally projected but at the same time the Federal Governments collection for Income Tax and Company Tax were growing at even greater levels due to the first wave of the very strong commodity prices courtesy of the China growth story.

Contrary to what was originally proposed when the States negotiated to establish the Federation the Central Government now has the strong financial muscle as it collects the major sources of revenue.

I appreciate that debate around the sharing of GST is a difficult one to address politically but when a State like Western Australia is rapidly heading towards receiving a zero share of the GST revenues something is amiss with the process.

In relation to GST revenues I make two observations:

1. There needs to be more transparency as to how the Grants Commission makes decisions in relation to the sharing of these revenues and

2. There is scope to broaden the base for the collection of the GST revenues.

**Proposal**

However, my proposal has nothing to do with the GST revenues but the sharing of the next generation of PRRT revenues flowing from the offshore LNG projects, four of which are currently under construction i.e. Gorgon, Wheatstone, Prelude and Ichthys.

**History**

The North West Shelf project in Western Australia is to date Australia's largest single most successful project. What most Australian's do not understand is that in an agreement negotiated between the State (Western Australia) and the Federal Government (Malcolm Fraser, Prime Minister) the royalties are split approximately 70/30. 70% to Western Australia and 30% to the Federal Government. With the operations of the Grants Commission much of that 70% is then redistributed to the other States so all the States benefit from the success of the Resource Sector in Western Australia.

With this next generation of offshore LNG projects, namely the ones under construction at present, Gorgon, Wheatstone, Prelude and Ichthys there will be no royalties flowing under the current arrangements to Western Australia or any of the other States. All of the PRRT from these projects will flow direct to Canberra.

**My proposal, my relief valve, is that the next generation of PRRT revenues streams from these offshore projects be shared 50/50 with all the States on a per capita basis. No Grants Commission involvement - just a simple, clearly understood sharing with no strings attached to the money.**

The beauty of this proposal is that the Central Government has 8-10 years to take into account that it is not going to have all of this massive revenue bonanza hit it books and the States similarly know they are going to start receiving access from new growth revenue streams which will enable them to have more autonomy and how they make decisions about the delivery of services that are their Constitutional responsibility.

This is how it works. When the Gorgon project, for example, comes into production approximately three years after that date the Federal Government gets a big hockey stick lift in

Company Tax collections – we have seen this with Woodside's Pluto project coming on stream recently.

Approximately 8 years after it comes into production there is a second hockey stick as the company starts paying its PRRT streams once all expenses associated with that project have been taken into account – <u>IT IS THIS HOCKEY STICK OF REVENUE THAT IM PROPOSING BE SHARED WITH THE STATES.</u>

I have tried unsuccessfully with successive Governments to consider this proposal. It will certainly be opposed by Sir Humphrey in Canberra and by many Federal politicians in both the Liberal and Labor parties who are attracted to the financial muscle being centred in Canberra.

This proposal is simple, fair and similar to the sharing already in practice for the North West Shelf project. The attached graph has been prepared by RISC, Australia's largest independent oil and gas advisory firm at which I am its Chairman.

These estimates of Company Tax and PRRT revenues can be updated and no doubt Treasury would have modelling in this regard.

As I have said at the outset I believe that this proposal is simple, practical and brings us back to the revenue sharing principles that the States agreed to before the Federation was agreed to.

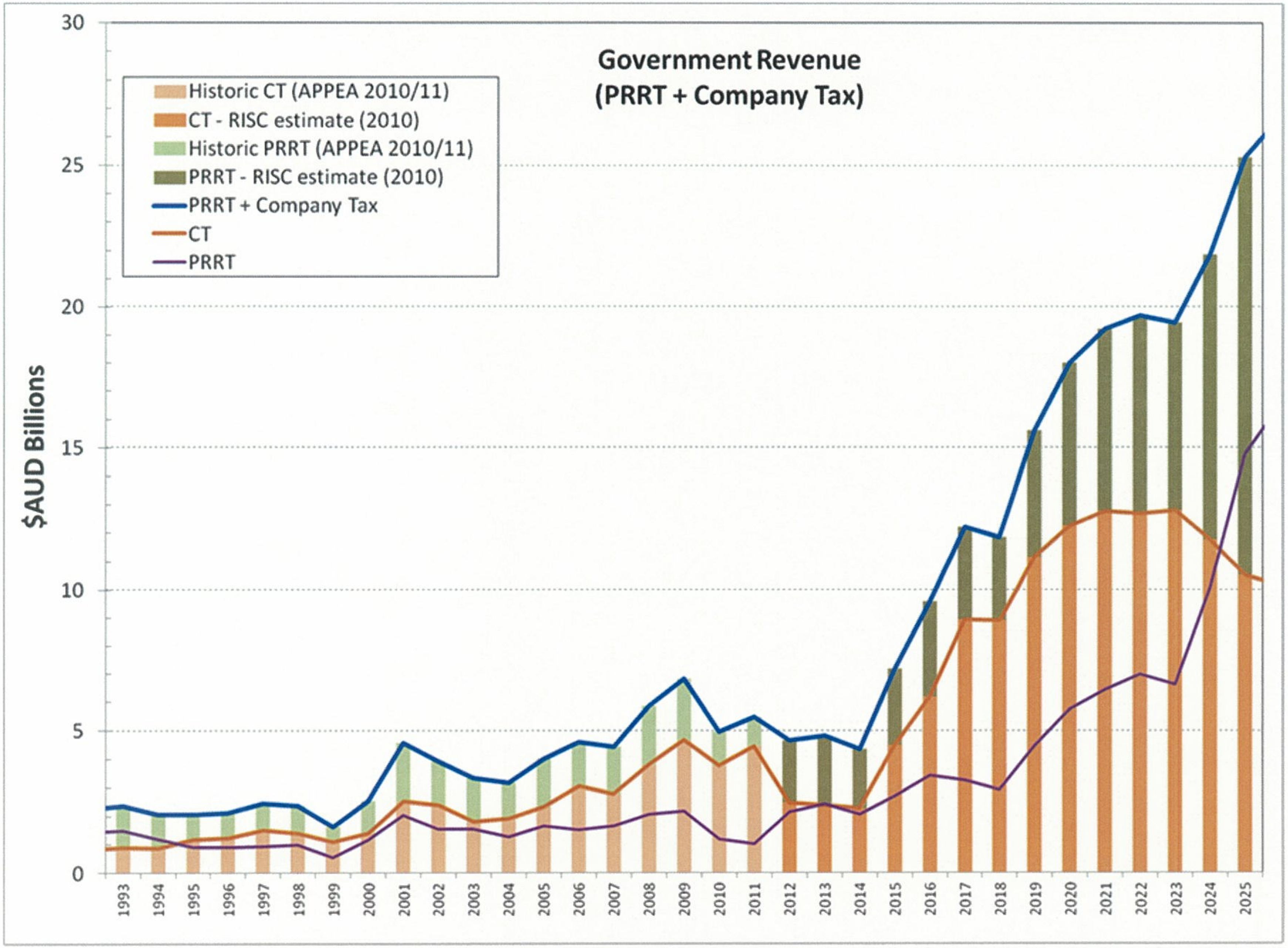
They provide adequate time for each level of Government to prepare for what is going to be a major new revenue stream for our Nation and it is a proposal that I believe would receive bipartisan support.

Thank you for the opportunity to present this to the National Commission of Audit.

Yours sincerely,

[redacted]

Richard Court
Premier & Treasurer of Western Australia, 1993 - 2001


Government Revenue
(PRRT + Company Tax)
Historic CT (APPEA 2010/11)
CT - RISC estimate (2010)
Historic PRRT (APPEA 2010/11)
PRRT - RISC estimate (2010)
PRRT + Company Tax
CT
PRRT
$AUD Billions
0
5
10
15
20
25
30
1993
1994
1995
1996
1997
1998
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RISC