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Fiscal federalism in Australia: Legal constraints and opportunities

Melbourne Institute

Economic and Social Outlook Conference

1-2 November 2012

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Road map

1. Constitutional framework for taxing and spending
2. State tax reform and horizontal fiscal equalisation
3. Legal constraints on federal spending
4. Federal institutions and legal opportunities

Constitutional power to tax

- Federal government has power to levy tax of any kind
 - “The Parliament shall ... have power to make laws ... With respect to taxation” (Sec 51(ii) of the Constitution)
- States have concurrent power to levy taxes
 - But are prohibited from levying tariffs, customs and excise (sec 90 of the Constitution)
 - Interpreted such that States cannot levy any sales taxes (including value added tax or Goods and Services Tax)
 - Since World War II (1942), no State has levied income tax although they have power to do so

Taxation

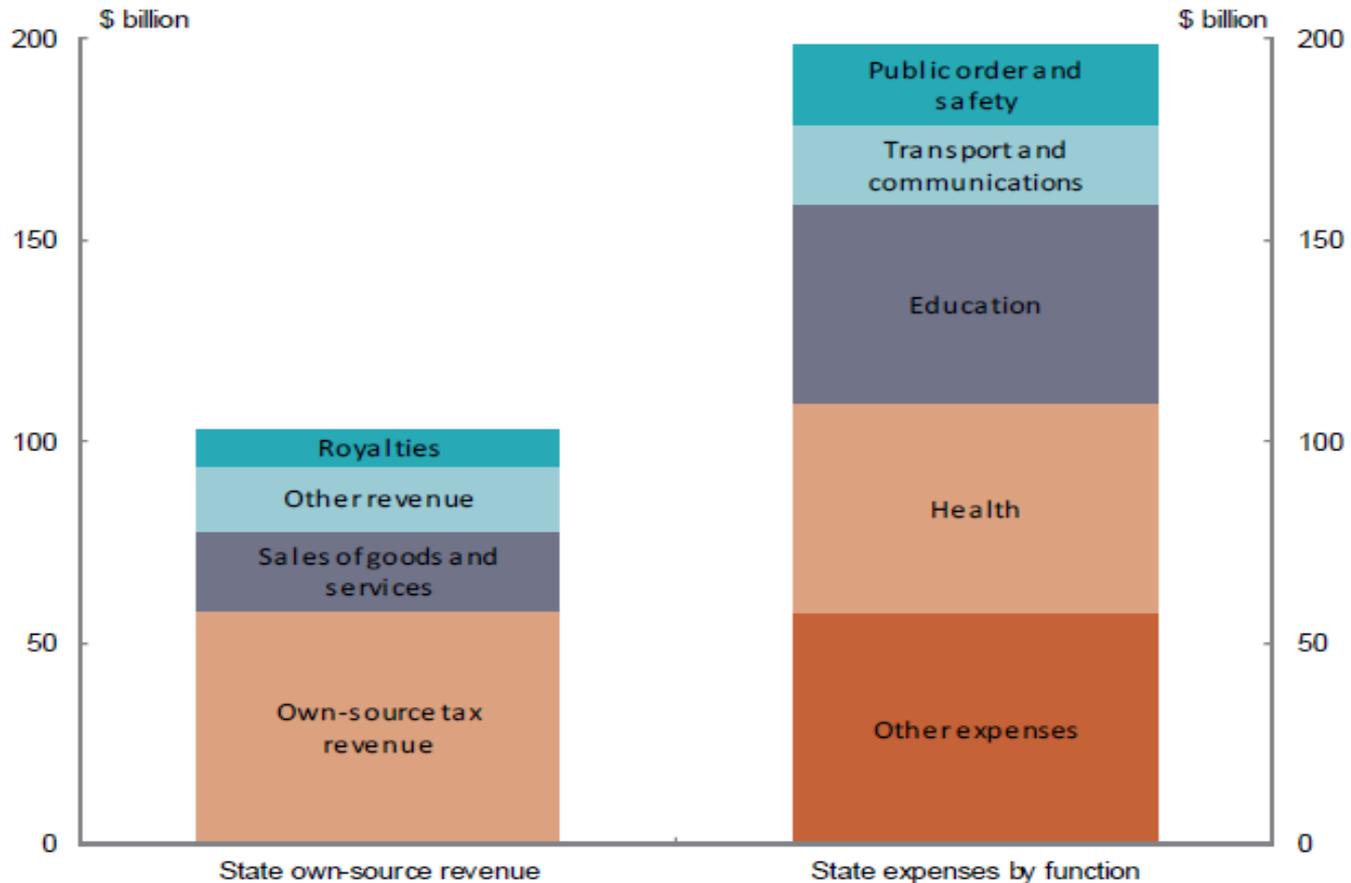
Table 7. Taxation Revenue % share by sphere of government and source of revenue 2010-11²⁰

	Federal	State	Local	Total
	%	%	%	%
Taxes on income	57.3	-	-	57.3
Employers payroll taxes	0.1	5.1	-	5.0
Taxes on property	-	5.8	3.5	9.3
Taxes on provision of goods & services	22.9	2.9	-	25.7
Taxes on use of goods & performance activities	0.2	2.5	-	2.7
Total	80.5	16.2	3.5	100.0

Source: Comrie (2012); ABS Taxation Statistics 2010-11

State revenues and expenses

Figure 1.2: Total State expenses and revenue, 2010-11



Source: ABS Taxation Revenue Australia, 2010-11, cat. no. 5506.0, ABS Government Finance Statistics, Australia, 2010-11, cat. no. 5512.0 and State financial statements.

Federal power to grant to States

- Under the Constitution:
 - Sec 96: “... the Parliament may grant financial assistance to any State on such terms and conditions as the Parliament thinks fit.”
 - Can discriminate between States in providing grants
- Eg, federal grants \$97.2 billion in 2009-10
 - 33% of federal revenues
 - 50% of State revenues
- Currently, three types of federal grant:
 - GST grants (fiscal equalisation)
 - Specific Purpose Payments (conditional grants)
 - Partnership Payments (conditional grants)

AFTS proposed State tax reforms

Review of Australia's Future Tax System, www.taxreview.treasury.gov.au

Table 1: AFTS Proposals for State Taxes

Tax	Revenues 2009-10 \$b	Proposal	Possible Replacement
Payroll	16.8	abolish	Consumption
Insurance	4.6	abolish	Consumption
Property transfers	12.3	abolish	Land tax
Land tax	5.8	Retain and reform	Modified base
Resource Royalties	6.6	abolish	Resource rent tax
Motor Vehicle revenues	7.0	Possibly abolish tax component	Road user charges
Gambling	5.0	Retain and reform	na

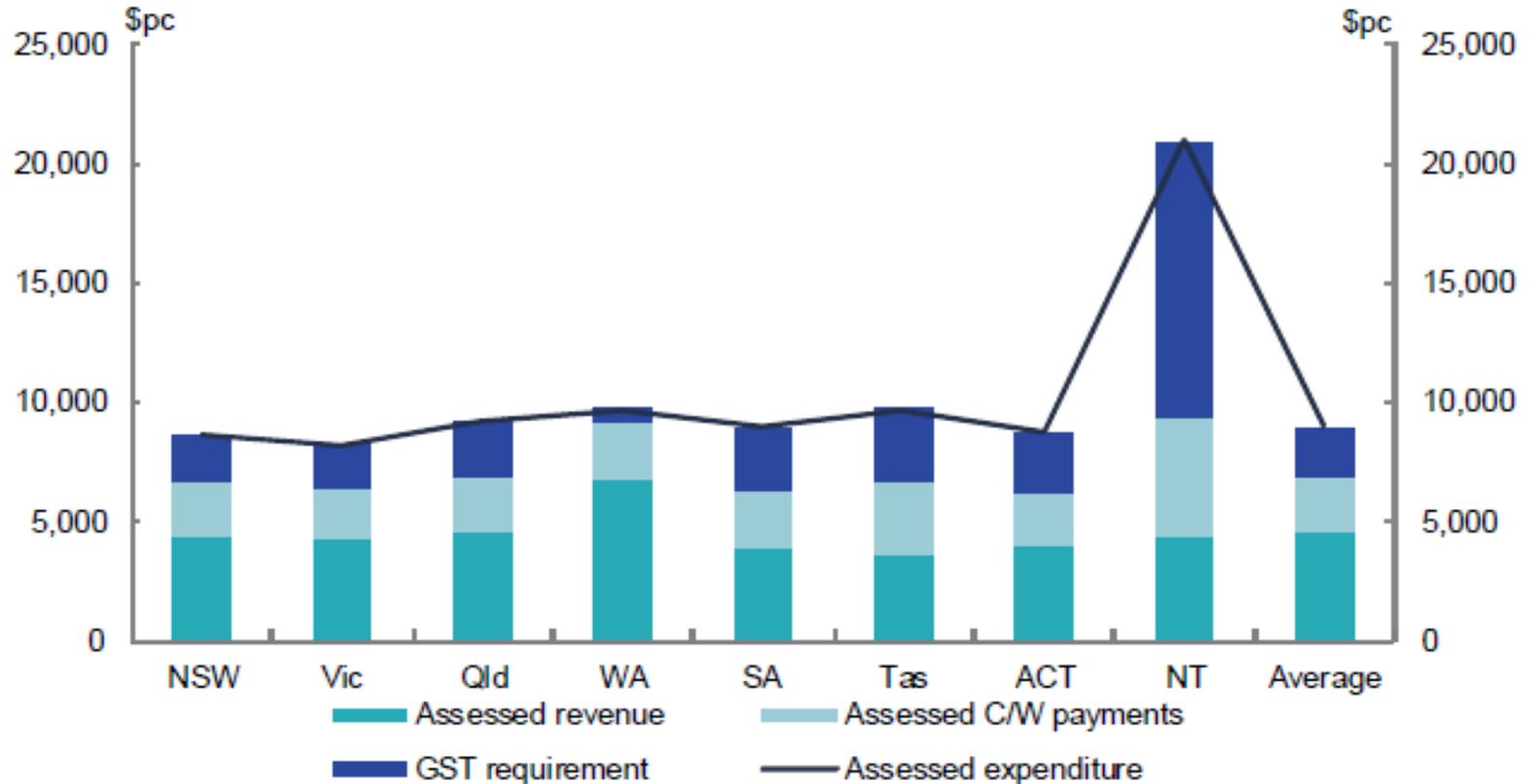
Source for revenues: Taxes, ABS Taxation Revenue Australia, 2009-10, Cat. 5506.0: Royalties, Commonwealth Grants Commission website (note significant royalty revenue increases are expected in coming years)

Horizontal fiscal equalisation

- GST revenues only are shared by HFE
- Objective is full equalisation of fiscal capacity
- Proportion of GST revenue that is shared:
 - Total GST revenue is approximately \$48 billion
 - Approximately 8% of total is redistributed
 - Remainder is granted per capita to each State
- Review of distribution
 - www.gstdistributionreview.gov.au
 - Final report expected in **October 2012**

Fiscal equalisation

Figure 1.2 GST requirement, 2010-11



Source: CGC, 2012 update

Source: GST Review Interim Report March 2012

Cth spending and regulatory power

- Limits on federal spending and regulatory power
 - Sec 81, 83: Federal power to appropriate monies to spend “for purposes of the Commonwealth”
 - Sec 51: limited legislative powers; sec 61 executive power
- High Court case authority
 - Historically, uncertain how broad was the federal government power to spend its revenues
 - Increasingly, federal governments have been utilising executive spending, with contracts as regulation
 - Recent cases indicate limits on federal spending power
 - *Pape* 2009; *Williams* 2012

Intergovernmental Agreement on Federal Financial Relations

- 1999: Delivers all GST revenues to the States
- 2009: New Agreement reorganises grant and conditions processes and governance
- COAG Standing Council on Federal Financial Relations
- National Specific Purpose Payments
 - Eg, in 2009-10:
 - Healthcare (\$11.2 billion);
 - Schools (\$9.7 billion);
 - Each SPP is associated with a National Agreement

Legal opportunities?

- The legal constraints on federal spending power, and on State taxing power, pose challenges
- There is an opportunity to reinvigorate the operation of section 96 grants to States; this places more pressure on the system of intergovernmental agreements but may strengthen State abilities to negotiate tax reform
- In the past, we have developed new cooperative institutions to deal with new federal challenges
- Is there an opportunity to do this in future?