

# **NSW Review of Federal Financial Relations**

**Submission by  
Jonathan O'Dea MP, Member for Davidson  
Speaker of the NSW Legislative Assembly**

## **1. Introduction**

In 1901 six self-governing British colonies united to form the Commonwealth of Australia to make decisions about issues concerning the whole nation. It was a controversial decision for people living in NSW at the time, as many felt NSW may lose power within the federation. Similarly today, many people living in NSW believe it does not receive its fair share of Commonwealth monies.

The federation has operated successfully since 1901, but the federation model requires updating to reflect the increasingly diverse character and prosperity of the states in the 21<sup>st</sup> century. As part of an ambitious agenda for NSW's future, I believe we need to reform the functional and financial responsibilities of different levels of government, especially where there is duplication at both state and federal levels. This is the focus of my submission.

## **2. Financial relationship between Federal and State governments**

The interdependent financial relationship between the Australian Federal Government and the states, including NSW, continues to be a key feature of our Australian Federation. In 2017-2018, \$105 billion or 44% of all states' revenue came from the Commonwealth. In 2019/20, NSW expects 38% of revenue to come from the Commonwealth, including 22% from GST payments, 12% from National Agreements and 3% from National Partnerships.

This interdependent relationship was initially developed to ensure both levels of government maintained an ongoing co-operative relationship. Unfortunately the nature of the relationship has at times adversely effected service delivery for many Australians, due mainly to its administrative complexity. The relationship has also

created other problems for the states, including a growing financial dependence on federal funding, and stronger links between funding distribution and planned productivity enhancing reforms required by the Federal government. This has tended to stifle innovation by the states when delivering services and detrimentally affect citizen outcomes.

### **3. Delivering better value for money**

Does Australia's move towards a more centralised model of government represent better value for money and better outcomes for citizens?

The states are responsible for nearly half of government operating expenditure, but raise only 24% of their own revenue. In contrast, the Commonwealth raises more revenue than it spends. Due to this vertical fiscal imbalance, grants to states are used to help redress the imbalance.

The states need a more sustainable revenue base to decrease their financial dependency on the Federal Government. They also need to find ways to increase funds without raising taxes, spend money more efficiently and trial innovative new approaches to service delivery.

The continued uncertainty about how states are expected to financially support vital frontline services and the community's high levels of expectation from education and health services in particular, creates a long term dilemma for state governments. The inefficiency of a two tiered bureaucracy continues to rob funds from vital frontline services and does not represent best value for money for taxpayers.

### **4. Funding model simplification**

Federal funding arrangements, including National Agreements and Partnerships, can adversely affect how states manage their budgets, plan for the future and make spending decisions. The reasons for this include strict conditions applied by the Federal government about how money can be spent; ongoing funding uncertainty;

considerable time spent on negotiating the agreements; and misalignments of objectives between the two levels of government.

How can we simplify funding models, cut duplication and make processes and funding more transparent to citizens, while avoiding blame-shifting and cost shifting? It makes sense for one level of government to be responsible for funding each portfolio area. A prime example of this is the funding and delivery of health care and education where there is limited motivation for each level of government to address the bigger picture, plan for the future and save taxpayer money.

If the NSW government funded all education and accepted responsibility for its outcomes, it would save millions of dollars a year. This money could be better spent on hiring more teachers with improved training and empower the states to make innovative, long term decisions that raise educational standards. It would also enable a simpler, more efficient and transparent funding model to be developed.

The current funding model is complicated and difficult to understand, with both state and commonwealth governments providing funds. Government schools receive most of their public funding from state or territory governments, with supplementary funding from the Commonwealth; and private schools receive the majority of their funding from the Commonwealth government, with supplementary funding from state and territory governments.

Today, the states have primary responsibility for education, but there is a good case for the Commonwealth government completely vacating the education funding space. This type of reform would reduce duplication, increase efficiency, reduce the scope for arguments between different levels of government, be far simpler for people to understand and, most importantly, deliver better outcomes for the public.

Conversely, the Commonwealth government would fund health care ahead of education. The actual delivery of health services should remain at a more grassroots level, but with the federal government taking responsibility for future planning and outcomes. This would also better align with current Federal funding responsibilities for

Medicare, private health insurance rebates, pharmaceutical benefits, NDIA and aged care. This would constitute fundamental reform that would create clearer responsibility and accountability for driving further microeconomic reform in both health and education. It would also help address the vertical fiscal imbalance, as health expenditure grows at a disproportionately higher rate compared to other public expenditure – partly due to an ageing population, technology improvements, growing mental health problems and increased chronic disease management.

## **5. Conclusion**

NSW should aim to develop a more dynamic federalism that strongly supports our position in a constantly changing global world and ultimately delivers better value for taxpayers. We need an improved federalism which does not rely on higher or additional taxes and includes intergovernmental arrangements that benefit our constituents. In that context, as a large and wealthy portion of the Australian nation, NSW needs more trust and autonomy in decision-making processes and service delivery, and less bureaucracy and duplication so it is able to effectively operate in a modern, global economy. I strongly recommend fundamental intergovernmental reform of which level of government is responsible for funding health and education functions.