

**Vista 8**

**“How will the Federation look in 2020”**

**at**

**Government House Ballroom, St Georges Terrace, Perth**

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## **“How will the Federation look in 2020?”**

In addressing this subject I will unashamedly be talking from a Western Australia perspective, that is, how will Western Australia be positioned inside the Federation in the year 2020.

I am honoured to be invited to speak in this year's Vista Public Lecture Series on this subject.

Since leaving politics I have stayed out of the public limelight giving few public addresses, but much of what I say today in relation to the Federation I have said previously in smaller, private presentations.

As Premier I always reinforced the need to support a common goal of strengthening our Federation at a time when, in practice, we are witnessing its continual weakening with the insidious trend to centralise more power, including financial power, in Canberra.

Being politically even-handed it is both sides of politics that have been contributing to this trend.

Joel Fitzgibbon, the Federal Member for Hunter and the current Minister for Defence, said in presenting the Inaugural Edmond Barton Lecture this year, that an ideal reform of our Federation would be the abolition of the States.

At the time I said I could offer my 100% support for this proposition with just one proviso – that Western Australia secedes just prior to the States being abolished!

I love reminding people from the Eastern States that Western Australia is the only State that has never been a part of New South Wales. It would just take us back to that point in time in our history.

You might simply dismiss Joel Fitzgibbon's comments as that of a centralist Labor politician.

Sadly, it's a view shared by many Federal politicians from both sides of politics.

I attended a Mining Conference in Perth during the previous Federal Government's reign and the Minister, during question time, after delivering his opening address, said if he could be granted three wishes one of them would be for the abolition of the States as they are a nuisance.

When I pleaded with senior Ministers in the former Federal Government to agree to similar royalty sharing arrangements for the next generation of Western Australia's offshore oil and gas reserves similar to those agreed for the North West Shelf Project they sniggered, “Why would you want to give the States more money when they can't even handle what they've got.”

All of these comments, both from the previous Government and the current Government were made at a time when the Federal coffers were flush with funds

driven by the massive resource development projects in Western Australia and in Queensland.

And when you look at the success of these massive resource projects in Western Australia, the main contribution the Federal Government made was to finally agree to lifting the ban on exporting iron ore from this State back in the 1960's and the rest of it was largely driven by Western Australian State Governments with the vision to turn these development dreams into reality.

If a State Government is not performing the people simply change it as occurs on a regular basis. It's one of the great strengths of a Federal system.

My late father would always remind me when talking about the role of the States of what Sir Robert Menzies said after a Premiers' Conference and Loan Council Meeting,

“Six State Premiers send me up the wall, but I would not have it any other way because it is our insurance against dictatorship.”

The summary of my speech, “How will the Federation look in 2020” is simple – two thirds of Australia will be happy, one third – the Western third – will not be impressed.

Not impressed that after sixty years of remarkable resource developments from 1960 to 2020, guided and driven largely by respective State Governments, Western Australians will themselves feel exploited with not enough long term tangible benefits associated with this remarkable development.

In 2020 Western Australians will be questioning why a remote central Government in Canberra is now dictating and calling the shots, both from a financial and key policy perspective.

To predict where we will be in 2020 we need to understand what has happened historically.

One way to look at this issue is to take a snapshot of where Western Australia sits in the Federation at key points in time.

- 1900 at the beginning,
- 1930 during the Depression,
- 1960 just prior to the modern day resource boom,
- year 2000, and
- then in 2020.

1900

Western Australia's population was under 200,000.

The Australian Constitution was enacted and Royal Assent was given by Queen Victoria on 9<sup>th</sup> July 1900.

A referendum was held on 31<sup>st</sup> July 1900 in Western Australia to decide whether or not Western Australia should join this new Federation.

It was passed with the Yes vote significantly increased by voters on the Goldfields, many of whom had come to Western Australia from other States, including Victoria, as a part of our gold rush. Incidentally, it was the first time women were allowed to vote in Western Australia.

In the decade leading up to Federation, John Forrest our State's first Premier was involved in the delicate and often difficult negotiations, which initially also included delegates from New Zealand, as to how a Federation could be established. They had the responsibility of creating our Australian Constitution.

Commentators on our Federation suggest there are a number of important parameters associated with a successful Federal system and these include:

1. Federations work if there is an understanding they involve a delicate balancing of powers and the proper reflection of the unique features of a country, particularly a country as large as Australia;
2. It is critical that no one level of Government within our Federation has too much power;
3. Those who control the purse strings have the power and in just over 100 years we have seen too much financial muscle centred in Canberra with that trend continuing and that is not healthy; and
4. Competition between the States is imperative for our nation's well being – not Canberra telling the States what is best for them.

John Forrest's major concern was for Western Australia to be able to secure an ongoing independent, viable revenue base.

At the time of Federation, the States' main form of revenue was Customs and Excise duties which accounted for 76% of the country's taxation base.

It was agreed three quarters of that revenue would be returned to the States and that was written into the Constitution in Section 87. It was only for a ten year period.

We were not off to a good start!

As early as 1902, Alfred Deakin said the States were "financially bound to the chariot wheels of the Commonwealth".

In 1900 there were very good intentions for the States to maintain their independent and viable revenue base, but quickly this deteriorated.

In 1908, the Commonwealth Parliament, together with the High Court, ended payments to the States of the Commonwealth Surplus Revenue.

In 1910, the Commonwealth Parliament abolished its obligations to pay to the States three-quarters of all Customs and Excise Revenues raised by the Commonwealth.

Gradually these revenues were replaced by Commonwealth Grants of financial assistance which were not permanent or constitutionally guaranteed – their continuance dependent on the discretion of the Commonwealth.

In the 1920's there was a further re-interpretation of the Commonwealth Constitution by the High Court when the Commonwealth Parliament legislative powers were to be given a wide [rather than narrow] scope and meaning.

When applied to the External Affairs power decision in 1980's this has enabled the Commonwealth to use international treaties and conventions to override State laws and intrude into areas of State concern and responsibility.

### 1930

So in the three decades after Federation, with a population of around 400,000 there was growing dissatisfaction with the Commonwealth's fiscal and legislative dominance and control.

1930 we were in the Great Depression and just prior to this discontent coming to a head. In 1932 the Western Australian Government decided to hold a referendum on seceding from the Federation on the grounds of unfair financial treatment.

This referendum was held on 8<sup>th</sup> April 1933 and it was 2-1 majority in favour of secession from the Commonwealth.

On 24<sup>th</sup> May 1935 a Joint Select Committee of the House of Lords and Commons resolved it was not proper for the Western Australian petition to be received because the United Kingdom Parliament could – as a matter of Constitution priority – only dissolve the Commonwealth at the request, and with the consent, of the Commonwealth. That consent had not been provided.

This secession vote however sent a very clear message to the Federal Government that Western Australia was “not happy” and it led to the establishment of the Commonwealth Grants Commission. Its role involved making recommendations to the Federal Government for special grants to claimant States.

This is basically a system to ensure that all States were capable of providing the same standard of basic services.

In 1930, Western Australians were pretty grumpy with Canberra.

### 1960

If we move forward to Western Australia in 1960, we just had a new conservative Government elected in 1959 having gone to the polls with a very clear policy to develop the resource riches particularly in the north of our State. There were still only 700,000 people living in Western Australia.

Between 1930 and 1960 there had been another major change in Commonwealth/State financial arrangements. That is, during the second World War in 1942, after Pearl Harbour, Prime Minister Curtin asked the States to hand over their income taxing powers for the duration of the War with a guarantee they would be handed back at the end of the War. The Premiers refused.

The Federal Government then passed legislation to take over the States' income taxing powers for the duration of the War. The legislation was challenged in the High Court and the States lost.

After the War, then Prime Minister Chifley refused to hand the income tax back to the States, saying the High Court had ruled that the Federal Government could collect an income tax.

So, we have a situation where the States constitutionally can raise an income tax, but politically, if the Federal Government is not going to leave that field, it is virtually impossible to bring in an additional tax of this nature.

The States were compensated with what is now known as Financial Assistance Grants.

In 1960 we had been through the rebuilding after the Second World War and Western Australia was still a relatively small economy and a claimant State – or in other words mendicant State.

With very little help from the central Government, Western Australian then started to develop the resource riches of this State.

That is quite a remarkable story in that it was a policy developed and carried out by a State Government that had no money and had very little support from the central Government.

The State Government developed an interesting regime of State Agreement Acts where companies were given access to resources for development, but in return had to build all the basic infrastructure for those projects.

The massive iron ore projects in the Pilbara that today are still so crucial to our national economy, were largely designed, built, funded and operated by the private sector companies – what are now the Rio's and the BHP's.

Infrastructure that today is still a great export earner for this nation.

This laid the foundations for Western Australia to move from being a claimant State to a contributor State and the major driver behind our national economy with both mining and oil and gas export income to the point where Western Australia accounts for 35% of the nation's export income.

It is interesting to note that it was only in the 1970's with the Seas and Submerged Lands Legislation that agreement was reached between the State and Federal Government as to how these offshore waters would be administered with the concept of delegated authority to the States being introduced.

Like in so many other areas, the Commonwealth is becoming increasingly interventionist in the development of the Offshore Petroleum sector particularly the duplication of approvals for onshore processing facilities.

In effect, the State Government underwrote the North West Shelf Project by building the domestic gas pipeline to the southwest along with a “take or pay” contract and the royalty sharing arrangements saw the majority of those royalties – nearly 70% - flowing directly to the State Government as the State’s own source revenues. The balance went to the Federal Government.

## 2000

By the year 2000 we have experienced forty years of resource development. Population had more than doubled to nearly two million people.

Commodity prices are low but still providing good revenue flows to a State Government, shortly to be followed in the next decade by massive revenue flows when commodity prices lifted significantly.

People in the Eastern States in the year 2000 were arrogantly telling Western Australians our resource economy was yesterday’s story – old economy stuff. The new world was high tech. When the tech wreck came and commodity prices lifted, they quickly changed their tune.

Western Australia’s 40 year close relationship with our Asian neighbours was bearing fruit.

We had developed a mature relationship with Japan, Korea and Taiwan and pioneering new commercial links with China as its economy rapidly accelerated.

## 2020

We now move forward to 2020 – and let’s face it, we are nearly half way there, so now we are talking only twelve years into the future. This is where I am predicting we are leading to a situation where Western Australians will not be happy with their position inside the Federation.

For a large part of the first decade of the 21<sup>st</sup> century, we had a Liberal/National Party Coalition in Government in Canberra with all of the States electing Labor Governments.

We witnessed a rapid acceleration of the central Government concentrating more powers in Canberra seemingly on the basis that most wisdom in this country resides in that town.

We repeatedly heard the Federal Treasurer deriding the States saying, “What are you complaining about. We’ve given you a growth tax with the GST.” Then proceeding to tell us that this tax had grown at a far greater rate than was originally projected.

What he didn’t add was that the Federal Government’s income tax, company tax and capital gains tax collections were growing at an even faster rate than was projected

at the time, widening the gap which gave the Federal Government a growing percentage of total revenues collected.

Historically these will be seen as very buoyant times with company tax, capital gains tax, income tax at record levels and welfare payments with low unemployment at low levels.

With the central Government awash with funds they were constantly telling the States they should be doing more and promising to put in extra money towards roads, health, or education on the proviso the States matched it and spent it according to the Federal Government's terms.

I listened to very experienced, sensible Heads of State Departments saying how they found it demeaning to go to Canberra to put a case forward for additional support to be rejected because it didn't meet the political agenda of the Federal Minister.

So much for putting a value on local knowledge and keeping decision making close to where the action is.

We saw the Federal Government do what only a Labor Government could dream of and that is overriding industrial relations powers of the States and centralising it in Canberra – mind you, with the strong support of the business community.

The business community was saying that no future Labor Government would dare roll back the industrial relations reforms that had been put in place.

The changes introduced were what Gough Whitlam could only have dreamed of achieving. They removed a great deal of flexibility that had previously been a strength in our industrial relations system where there was competition between the State and Federal systems and the ability to move between the two systems.

For example, in 1993 the Western Australian Government I lead was able to bring about major changes in industrial relations which were quickly taken up by the resources sector. They resulted in significant improvements in wages, conditions and a massive cut in industrial disruption, particularly in the resources sector.

All this was achieved while the Keating Labor Government was in power federally.

Now with all this power centralised in Canberra, if you don't like the system they impose, well "stiff bikkies".

It is interesting that during these challenging economic times we are now seeing the return of industrial disruption in the Pilbara under these changes.

In summary, during the large part of the first decade of this century we have had "boom" years which have seen more financial muscle growing in Canberra.

I go back to the initial comments I made about a Federation and that is,

"Federations only work if there is an understanding they involve a delicate balancing of powers and the proper reflection of unique features of a country, particularly a country as large as Australia".

Now we have, as we speak, the world facing a global financial crisis. We reached a point in recent weeks where the global finance mechanisms were on the point of collapse.

Kevin Rudd, our Prime Minister, has come out and declared, "We have the economic equivalent of a national security crisis."

During the second World War when we had our last major security crisis we saw the central Government temporarily take over the States' income taxing, never to be returned. During this current national security crisis, what say will the States have in the recession proofing policies being proposed?

And I suggest we will see major decisions being made out of Canberra with very little input, in practice, coming from the State Governments.

The large surpluses that have been quite properly amassed during these "boom" years and that is to the credit of the previous Coalition Government, are now to be deployed in our modern version of Keynesian economics. These large surpluses were largely from a very successful economy capitalising on strong global commodity prices.

The buzz word now is to "pump prime" the economy.

Most of the money for the "pump priming" is in the hands of the central Government and they have announced a number of infrastructure programs but making it clear they will be making the decisions as to where most of this money will be spent.

Infrastructure Australia will make recommendations to the Government for major infrastructure works from the Building Australia Fund but with the Federal Government having the final say.

Now they have announced they are going to replace the former Government's Regional Partnerships program, which they heavily criticised, with a new Regional and Local Community and Infrastructure Fund. This will enable them to go over the top of the States and deal directly with Local Government – and the old favourite of Canberra – regional funding.

It reinforces the old saying, "He or she who has the money calls the shots" and the way our Federation has evolved, central Governments have the financial muscle and they will try and make the maximum political advantage as to how those funds are distributed.

My concern is that it could easily lead to rewarding those States who have been the least effective in running their economies during the good years.

These are the States who have not encouraged investment in productive infrastructure - it will be the squeaky wheel getting the oil.

Whereas States like Western Australia who have developed very internationally competitive, productive infrastructure could well be penalised.

Western Australia simply does not have the political numbers to be effectively heard at the centre of Canberra.

If the current path of our Federation continues, in the year 2020 Western Australia will be receiving just a 5% share of what is being distributed by the Commonwealth Grants Commission with over 10% of the population.

We will be penalised for our success. The time has now come for there to be a re-assessment of the formula by which the Grants Commission distributes funds to the States. A new assessment of the special requirements in such a large State that has the runs on the board in delivering economic success to our national economy is long overdue.

I want to conclude by highlighting the major concern I have for our State in the year 2020 and that is the failure, to date, of the State Government to negotiate royalty sharing arrangements for the next generation of major offshore gas projects similar to that negotiated for the North West Shelf Project.

Most Western Australians are simply not aware that the majority of the royalties paid by the North West Shelf Project – nearly 70% - flow directly to the State Government as own source revenues, with 30% being collected by the Commonwealth Government.

The Commonwealth Grants Commission then takes into account these royalty revenues and as a result, as mentioned earlier, we receive a lesser percentage of the pool, but we do get to keep approximately a net 10% which is critical in helping to build the key infrastructure required for this growing economy.

Under this system the other States and Territories become direct beneficiaries. It is a very fair way to distribute this royalty revenue.

But the next generation of major offshore gas projects, for example, the Gorgon project and the Ichthys project off the Kimberley, not a single dollar – zero royalties – will flow to the State.

During my time in Government I raised this matter with the Coalition on several occasions and I was told that when the Gorgon project came up for formal approval they would consider this matter.

It did not come up for formal approval in my time, but when it did, the hard negotiations between the State and the Federal Government obviously did not occur. The equivalent negotiations for the North West Shelf Project were initially between my father and Gough Whitlam with the proposals not favourable to the State and were finally concluded with Malcolm Fraser with a satisfactory sharing arrangement agreed to.

Similarly, with the Ichthys project in the Kimberley.

It is not an issue for the companies to resolve. It goes to the core of fair revenue sharing within our Federation.

So, in the year 2020 we will have a situation where the North West Shelf will be a mature Project and with finite reserves it will start moving into declining production and the next generation of projects, hopefully will have been built and all of those revenues will be flowing directly to the central Government.

It is in the best interests of all the States and Territories to support a Western Australian push for this royalty sharing as they all win – the more direct royalties Western Australia receives, the bigger the share of the Grants pool they receive.

Royalties for the Regions captured the imagination of Western Australian voters.

As I said at a function last week, we had a Royalty for the Regions program but Treasury called it a different name. They called it “Hendy Cowan”

Well, if you think there was a bit of heat generated at the last State election re the regions receiving a fair go, in 2020 a central Government that does not take into account the very real concerns being raised by Western Australians in relation to a fair sharing of these royalties, will be intense.

I am not advocating secession, but if you read “The Case for Secession” which is very thick and “The Case Against Secession” which is very thin that was prepared in the 1930’s, the case for secession today will be even stronger if this financial imbalance is allowed to continue.

States don’t always get it right but if the local people don’t like what they are doing in the delivery of essential services, you just change the Government in that part of Australia.

As Canberra becomes more powerful its lack of understanding of the different States’ special needs becomes accelerated.

In my experience many of Canberra’s key decision makers simply have not been to Kalgoorlie, the Pilbara, and the Kimber

They cannot comprehend the distances involved, the capital investment that has been made, the climate, the environmental and indigenous issues to be addressed. Putting it bluntly they are often incredibly naive and ill-informed except for one thing - if they visit Perth they know exactly what time the earliest possible flight that can take them back East leaves!

On the other hand, however, they don’t mind receiving the revenue streams. They can certainly count dollars flowing into Treasury.

Next time you hear a luminary from the East suggest the abolition of the States gently remind them that the States created the Federation, not the other way around, and one of those States produces 35% of this nation’s export income – it is a State that operates in the real economy – so be fair to the State. Not generous, just fair in how that State is treated.