

## **Submission to the Senate Select Committee on Administration of Sports Grants, February 2020**

### **Title: *Wrong Way, Go Back: Reforming Commonwealth Discretionary Grant Programs***

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This submission addresses the last item in the terms of reference:

1(f) any related programs or matters.

## Key points

- The primary objective of government spending at all times should be maximising value for money for taxpayers. Commonwealth discretionary grant programs in areas of state and local government responsibility, such as the Community Sport Infrastructure Grant Program (CSIGP), are particularly problematic because they:
  - entail significant political, financial and constitutional risks;
  - allow Commonwealth Ministers to make spending decisions that cut across the spending decisions of lower levels of government, contrary to the well-established public finance principle of subsidiarity;
  - involve high program administrative costs, many relatively small payments to grant winners, and wasted time and effort for the many losers; and
  - tend to distract the attention of Ministers, their staff and public servants away from their core national and international responsibilities, particularly during election years.
- Overall, programs such as the CSIGP are wasteful and inefficient compared to other ways of assisting lower levels of government to meet demand in their communities for infrastructure and other services.
- Therefore, the Committee could consider recommending a reform package that includes seeking bi-partisan support for:
  - confining Commonwealth discretionary grant programs to expenditure areas that have a clear line of sight to matters listed in Section 51 of the Australian Constitution;
  - not creating new discretionary grant programs in areas of state and local government responsibility;
  - allowing existing discretionary grant programs in areas of state and local responsibility to terminate;
  - a new focus on policy measures aimed at simplifying federal financial relations and improving the capacity of lower levels of government to meet demand for state and local services, including infrastructure services; and
  - ongoing training for all Members and Senators, their advisers and public servants to raise their awareness of the Australian Constitution and federal financial relations, and to improve the quality of policy advice.

## Constitutional risks

Political embarrassments over the past decade, which have reduced voters' trust in politicians, have often resulted from a lack of awareness of the Australian Constitution and populist election policies that have resulted in poor outcomes for taxpayers. Following successful High Court challenges relating to Commonwealth funding of school chaplains in 2012 and 2014, the Commonwealth Government ('the Commonwealth') converted the national school chaplains program into a national partnership program funded under Section 96 of the Constitution, and reported in Budget Paper No.3 (BP3), *Federal Financial Relations*.<sup>1</sup> Chordia, Lynch and Williams (2015) note that programs concerning the environment, regional development, local government, sport and the arts also do not obviously correspond to a head of Commonwealth legislative power in Section 51 of the Constitution. They observed five years ago that the Commonwealth did not appear to have taken any steps to restructure the range of other programs that may be similarly vulnerable to constitutional challenge.

I am not aware of the extent to which other Commonwealth programs have been restructured over the past five years and whether there has been a push back in the creation of new discretionary grant programs in areas of state and local responsibility. However, payments relating to the CSIGP – a new program since 2014 – have not been reported in BP3 and the corresponding section of the Final Budget Outcome (FBO, Part 3). In other words, funding has not been reported as Section 96 grants and the CSIGP does not correspond to a head of power in Section 51, so it appears 'stranded'.

Several factors may have contributed to this: first, the process of classification of payments; second, the current Federal Financial Relations Framework; and third, possible resistance to relinquishing discretionary spending powers. These are discussed in turn below.

First, the Australian Government Department of Finance (Finance) provides guidance to all Commonwealth entities on classifying payments as 'Commonwealth own purpose expenses' (COPE); payments 'to the States'; payments 'through the States'; and payments 'direct to local government authorities' (Finance 2019). Payments classified to each of the last three categories are reported in BP3 and Part 3 of the FBO.<sup>2</sup>

Finance's guide (page 5) includes two criteria for determining the dividing line between COPE and the other three categories: contestability; and the nature of transactions. Agencies often need further advice from Finance to determine the appropriate category.

It appears that the Australian Sports Commission has classified the CSIGP as COPE, when I believe the appropriate category would be payments 'through the States'. While many of the CSIGP payments have been directed to local councils as well as to non-government sports organisations, it is preferable that Commonwealth spending programs have only one

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<sup>1</sup> Williams v. Commonwealth of Australia and Ors [2012] and Williams v. Commonwealth of Australia & Ors [2014].

<sup>2</sup> The categories 'to the States' and 'through the States' relate to the six States, the Northern Territory and the Australian Capital Territory.

classification type to minimise administration costs. Further, in my view, classification of Commonwealth payments as 'direct to local government authorities' is not consistent with the Australian Constitution, which recognises only two tiers of government: the Commonwealth and States. Local government, the third tier, is established under the governments of the six States and the Northern Territory; the Australian Capital Territory Government administers both state and local government functions.

Misclassification of the CSIGP as COPE suggests there could be other Commonwealth discretionary grant programs in a similar situation. Identifying these would most likely involve a time-consuming troll through portfolio budget statements and agency annual reports, and cross checking candidates against listings in BP3.

Second, Finance's guide to classifying payments (page 4) also advises Commonwealth entities that payments to and through the States for general and specific purposes have been centralised under the Federal Financial Relations Framework administered by the Commonwealth Treasury since 1 January 2009. Previously, these payments usually went from Commonwealth line departments to their state/territory counterparts, by-passing the state/territory treasury departments.

It is worth noting that centralisation of payments through the Commonwealth Treasury to state and territory treasury departments was established at a time when there was a major new policy thrust to rationalise the number of payments for specific purposes to and through the States. This initiative failed to achieve its objective. Burdened by the continuation of many payments 'to the States' for specific purposes, state and territory treasuries have eschewed dealing with additional small payments relating to discretionary grants agreed or decided by Commonwealth Ministers when classified as 'through the States'. Further, since 2008-09, payments classified as 'through the States' have not been separately identified in BP3 and FBO tables by the Commonwealth Treasury.

Restructuring discretionary grant programs to manage constitutional risk invariably involves transferring discretionary power from a Commonwealth Minister to the States, as occurred when the school chaplains program was converted to a national partnership agreement. A third factor that may have contributed to the CSIGP being classified as COPE is possible resistance to relinquishing this power. Continuation of discretion at the Commonwealth level also implies more resources for administration in line agencies.

### **Political and financial risks**

However, there are other good reasons why Commonwealth Ministers should relinquish discretionary powers in this area of spending. First, discretionary grant programs in areas such as sport, local government, the arts, regional development and the environment are notorious for entrapping Ministers into acts of political greed, notably 'pork barrelling', during what is a relatively short federal election cycle. Once entrapped, there is then a strong incentive to try and cover up what are, in effect, egregious abuses of power and public trust.

Second, to the extent that a Commonwealth Minister uses his/her discretion to allocate funding for less worthy projects in marginal and/or targeted electorates, financial risks are ignored. These include, for example, possible class actions in the Courts, the costs of

defending challenges in the High Court, and an additional call on current taxpayers, or future taxpayers if new borrowings are required, to fund higher ranked projects of the losers.

Third, additional financial risks for the Budget may arise because the Prime Minister and other Cabinet members are distracted for an extended period of time from their core national and international responsibilities, and also because investigative journalists are not focussed on other more important spending issues and audit reports. Most Australians know about the so-called 'Sports Rorts Affair' now, but how many are aware that the estimated cost of acquiring twelve new submarines by design and construction in Adelaide blew out from \$50 billion to \$80 billion between 2016 and 2019? (ANAO 2020b).

### **More effective ways of funding state and local infrastructure**

A very strong case can be made for ceasing all discretionary grant programs in areas of state and local government responsibility and instead ensuring that the States and their local governments have adequate taxation powers, general purpose funding and/or block grants for specific purposes, consistent with the public finance spending principle of subsidiarity. As outlined by the Productivity Commission (2017), under this principle, responsibility for a particular spending function should, where practicable, reside with the lowest level of government given:

- sub-national governments are likely to have greater knowledge of the needs of citizens and businesses affected by their policies;
- with decentralisation of responsibility and decisions it is easier to constrain the ability of elected representatives to pursue their own agendas to the disadvantage of citizens they represent; and
- mobility of individuals and businesses exposes sub-national governments to a reasonable degree of intergovernmental competition (competition is an important driver of better performance).

In the case of funding community sports infrastructure, local councils have local knowledge about the needs of their communities and it is not surprising that many councils competed for grants under the CSIGP. However, it is worthwhile asking whether it is a good use of councils' administrative resources (funded by ratepayers) to be applying for grants under the various Commonwealth discretionary grant programmes.

Further, a local council or state government seeking to promote as much physical activity as possible to tackle obesity and to improve the mental wellbeing of its citizens would be highly unlikely to provide funding for shooting (or for archery and horse riding). The CSIGP appeared to adopt the broader definition of sport used by the Olympics.

### **The financial position of different levels of government**

Annual government finance statistics for the three levels of government in Australia are published by the Australian Bureau of Statistics with a lag of around 10 months. The latest statistics are for 2017/18 (ABS 2019). These indicate that the local general government sector as a whole was in a cash surplus position for several years up to and including 2017-18, in contrast to the deficit positions of the Commonwealth and state general government sectors.

Local councils are benefitting from increasing property values in a low interest rate environment. Also, women mayors are now making a very strong contribution to improving the performance of local government.

When local councils do not perform, for example because of a major spending scandal, they are usually sacked by the state government and replaced by an administrator. When a Commonwealth Government is afflicted by a spending scandal relating to an area of state and local responsibility, the root causes may not be addressed.

### **Training**

The Commonwealth Parliament and public service now have the opportunity to use the CSIGP as a case study for several training purposes: to raise awareness of, and respect for, the Australian Constitution; and to raise awareness of the current Federal Financial Relations Framework, and the how Commonwealth payments are classified. This training is very important for improving the quality of public policy advice, particularly in the area of federal financial relations.

### **Conclusion**

This submission aimed to highlight the structural cause of the so-called 'Sports Rorts Affair' as distinct from the many symptoms. The main cause is the continued ability of Commonwealth Ministers to establish discretionary grant programs in areas of state and local government responsibility, notwithstanding the significant constitutional, political and financial risks associated with these poor spending proposals.

Instead, Australian taxpayers would benefit greatly from real reform of federal financial relations. This is becoming more important as governments confront new spending pressures arising from higher annual growth in numbers of Australians aged 85 years and over each year from the early 2020s, and increasing expenses associated with adaptation to climate change.

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