

GPO Box K 845
PERTH WA 6842
PHONE (08) 9321 1925
FACSIMILE (08) 9321 1798

COUNCIL FOR THE NATIONAL INTEREST

WESTERN AUSTRALIAN COMMITTEE



House of representatives Standing Committee on
Economics, Finance and Public Administration

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A SUBMISSION

TO The Secretary
Inquiry Into Local Government
And Cost Shifting
House of Representatives
Standing Committee on Economics, Finance and Public Administration
CANBERRA ACT 2600

DATE 26 June 2003

EXECUTIVE SUMMARY

This submission addresses broadly, all of the Terms of reference and argues that it is time to call a halt to the existing arrangements for Commonwealth and State funding to Local Government.

The clear implication of the terms of reference and of the discussion paper, February 2003 "At the Crossroads" if followed to a logical conclusion would be to achieve a further weakening of the Federation contrary to the letter and spirit of the Australian Constitution, without reference to the people, and to centralise more power in Canberra.

The further implication and, ultimately the logical outcome of such a course, is the eventual replacement of State Governments by Local (regional) Government directly funded by the Commonwealth.

This is not in the national interest. If however, a case can be made out that it is in the national interest, then that case should be put to the people in the form of a referendum, as required by the Australian Constitution, rather than in the form of this Inquiry.

BACKGROUND

In the lead up to and at the time of Federation, our founding fathers recognised, very clearly, that a national government was best placed to determine national priorities, but recognised, equally clearly, that the State governments were far better placed to determine local priorities, and far better placed to determine the most effective way to deliver services to their citizens.

Unfortunately, in our view, the wisdom of these timeless principles, understood clearly by our founding fathers, has been ignored. For example the Constitution left sole responsibility to the States for, among other things, law and order, the regulation of commerce and industry, transport services, natural resources including land, essential services such as water supply, sewerage, drainage, electricity and gas, local government, education, housing, health and the environment. Centralisation of tax powers, combined with the Commonwealth's ability to make tied grants to the States, has seen the Commonwealth intrude into all of these areas of State responsibility, in some cases to the extent that the Commonwealth has usurped the States' role for all practical purposes. This creeping process of centralisation of power has been aided and abetted by the Commonwealth appointed High Court's interpretation of the Constitution.

HIGH COURT DECISIONS OF GENERAL APPLICATION

High Court decisions since 1908 have supported the trend to centralisation.

1908 *NEW SOUTH WALES V COMMONWEALTH*

The High Court held valid Commonwealth legislation which directed that money in excess of Commonwealth requirements for the financial year should be paid into trust funds for defraying the costs of services in succeeding years. Therefore, such money would not form part of any surplus revenue distributable among the States under Section 94 of the Constitution. As a result, the Commonwealth has ensured that there is no surplus revenue to be distributed to the States as the Constitution envisages in Section 94.

1920 *ENGINEERS' CASE*

This case established that Commonwealth powers should be interpreted broadly. The effect was that Commonwealth powers were expanded. This has permitted Commonwealth laws to intrude into areas which would otherwise have been subject to State control. In particular, the case held that

- (1) Commonwealth legislation can bind the Crown in right of a State. One consequence has been that the Commonwealth is able to impose taxes on the States (eg payroll tax, fringe benefits tax).
- (2) Commonwealth legislative powers listed in Section 51 of the Constitution are to be interpreted broadly and generally without taking into account State legislative powers or the effect of such a broad interpretation on State powers.
- (3) Commonwealth industrial awards can bind State instrumentalities.

The case was further evidence of the High Court taking constitutional amending and law-making powers to itself.

1926 *VICTORIA V COMMONWEALTH (ROADS CASE)*

This case held in making Section 96 grants to States the Commonwealth may attach terms and conditions to the grant of monies which are -

- (i) outside the area of Commonwealth legislative powers; and
- (ii) within State legislative and policy domains; and

One consequence of this is that the Commonwealth can dictate and control State policy.

1942 *SOUTH AUSTRALIA V COMMONWEALTH (FIRST UNIFORM TAX CASE)*

This case enabled the Commonwealth to become the dominant revenue raiser in the federation. The States were forced to relinquish income tax as a source of revenue.

1965 *FAIRFAX V COMMISSIONER OF TAXATION*

This case permitted the Commonwealth to impose a liability to pay income tax and then exempt from the tax if specified conditions (normally within State control) were met.

1971 *STRICKLAND V ROCLA CONCRETE PIPES LTD*

The High Court indicated that the corporations power - in Section 51(xx) of the Constitution - should be given a wide interpretation so that it would apply in relation to intra State matters previously governed by State domestic laws.

**1975 NEW SOUTH WALES V COMMONWEALTH
(SEAS & SUBMERGED LANDS CASE)**

Until 1975 it was accepted that the States' territorial boundaries ended three nautical miles from their coastline. In this case the High Court held that:

- (1) Offshore boundaries of States ended at low water mark and did not extend over the 3 mile territorial sea.
- (2) Commonwealth legislation - the Seas and Submerged Lands Act 1973 - gave sovereignty over territorial waters (including the seabed and airspace) to the Commonwealth, not the States.

As a result, the States' powers with respect to the territorial sea (including minerals, fisheries, navigation) no longer rest upon State legislative power, but upon Commonwealth legislation enacted pursuant to the 1976 Offshore Constitutional Settlement.

**1976 MURPHYORES V COMMONWEALTH
(FRASER ISLAND CASE)**

Despite State development permission having been granted, this case permitted a Commonwealth Minister to control the mining of mineral sands in Queensland by making the grant of an export permit conditional upon the mining company complying with environmental standards. The case held that

- (1) Commonwealth legislation can be valid even if it includes conditions designed to achieve ends in themselves outside Commonwealth legislative power.
- (2) The overseas trade & commerce power of section 51(i) of the Constitution was validly exercised in Commonwealth regulations to prohibit (on environmental grounds) exports of mineral sands, mined in Queensland.

Not only are Commonwealth powers interpreted broadly (following the *Engineers' Case*), but also when using those powers Canberra can attach conditions to regulate matters which go beyond even that broad interpretation of Commonwealth power.

**1979 R V FEDERAL COURT OF AUSTRALIA;
EX PARTE WA NATIONAL FOOTBALL
LEAGUE (INC) (ADAMSON)**

The High Court held that a non-profit organisation - a Western Australian League football team - incorporated under the *Associations Incorporation Act 1895* came within the corporations power - Section 51(xx) - and was therefore validly subject to the *Trade Practices Act* (Commonwealth).

1982 KOOWARTA V BJELKE-PETERSEN

This case (following *Engineers'*) gave a wide interpretation to the words "external affairs" in Section 51(xxix) of the Constitution. This enabled the Commonwealth, by relying on an international treaty, to make laws governing human rights which had previously been considered to be a matter for State Parliaments and the common law. As a result, Australia is subjected to international standards and criteria without the possibility of local needs and conditions being taken into account by State Parliaments and laws.

In particular, this case held that

- (1) the external affairs power supported the *Racial Discrimination Act 1975* (Clth) which implemented the UN Convention on the Elimination of all Forms of Racial Discrimination 1965.
- (2) Queensland policies, regulations etc concerning land (eg granting of pastoral leases) became subject to the *Racial Discrimination Act*.

**1983 COMMONWEALTH V TASMANIA
(TASMANIAN DAM CASE)**

This case gave a broad interpretation to Sections 51(xx) - corporations power - 51(xxvi) - race power - 51(xxix) - external affairs power. The High Court

- (1) upheld the validity of the World Heritage Properties Conservation Act 1983 (Clth) which -
 - (a) implemented the Convention for the Protection of the World Cultural and Natural Heritage; and
 - (b) prevented Tasmania building a dam.
- (2) indicated that Section 51(xx) permits

the Commonwealth to regulate the non-trading activities of a trading corporation undertaken for the purpose of its trading activities such as the Tasmanian Hydro Electricity Commission's preparatory work to construct a dam to generate electricity to sell.

- (3) State statutory authorities could be trading corporations for the purposes of Section 51(xx) and therefore subject to Commonwealth legislation.

Because most economic activities in a State are carried out by trading corporations, this case may enable the Commonwealth to regulate those activities and associated activities. Consequently, the Commonwealth may have power over virtually all aspects of business and associated activities (eg trading activities, working conditions, wages and salaries, safety standards). These are matters that have been governed by State laws and policies.

1986 RE LEE EX PARTE HARPER

This case indicates that virtually all employment relationships can be governed by Federal awards. For example, school teachers employed by the State in State schools can be bound by a Federal industrial award governing their terms and conditions of employment, including pay scales and hours of work.

1988 RICHARDSON V FORESTRY COMMISSION (TAS)

This case (following the Franklin Dam case) reinforced the Commonwealth's ability (by international treaties) to legislate on matters within States relating to the environment. The Court held that Section 51(xxix) supported the validity of a Commonwealth Act establishing a commission to inquire into and report on the possible identification, delineation and eligibility of an area of land in Tasmania for World Heritage and to protect that area (4.5 percent of Tasmania) from any intrusion.

1989 QUEENSLAND V COMMONWEALTH

This case expanded the range of environmental matters in which the Commonwealth could override existing State policies and laws. The High Court held Section 51(xxix) supported the validity of a Commonwealth law permitting Commonwealth identification and nomination of Queensland rainforest for world heritage listing. It also supported Commonwealth regulations prohibiting, without Commonwealth Ministerial consent, activities in that area, for example, road and forestry work.

1992 MABO V QUEENSLAND (No 2)

For the first time the High Court recognised common law native title to land. Matters concerning title to land and land laws have always been within the jurisdiction of State Parliaments.

HIGH COURT DECISIONS PARTICULARLY AFFECTING STATE TAXING POWERS

(Important cases are underlined)

1904 PETERSWALD V. BARTLEY

- . This was the first time the High Court examined the Constitution's prohibition on the States imposing excise duty.
- . The High Court adopted a narrow interpretation of excise duty by deciding that licence fees imposed by States on breweries were not excise duties.
- . Under the narrow interpretation, excise duty was a tax specifically on the quantity or value of goods produced in the State. States could therefore apply a tax on goods which did not discriminate between goods produced within the State and goods produced outside the State.

1904 D'EMDEN V. PEDDER

- . The High Court examined the power of the States to impose taxes on Commonwealth activities.
- . The High Court ruled that the Tasmanian Government could not impose stamp duty on a receipt given for the salary of a Commonwealth postal official.
- . It should be noted that a 1904 High Court ruling (*Deakin and Lyne v. Webb*) which held that a State could not impose income tax on the salaries of Commonwealth public servants, was later overruled by the Privy Council.

1908 WIRE NETTING CASE (KING V. SUTTON) & STEEL RAILS CASE (A.G. NEW SOUTH WALES V. COLLECTOR OF CUSTOMS)

- . Confirmed that the Commonwealth could impose customs duty on imports by State Governments, despite the Constitutional prohibition on the Commonwealth taxation of State property.

1911 OSBORNE V. THE COMMONWEALTH

- . Commonwealth land tax ruled valid.

1916 FAREY V. BURVETT

- . The High Court ruled that a Commonwealth order under the War Precautions Act fixing the price of bread was valid.
- . In this case, the High Court gave a wide interpretation to the Commonwealth's defence power under the Constitution. The Commonwealth's defence power was used in 1942 to take over the States' income tax administrations.

1920 AMALGAMATED SOCIETY OF ENGINEERS V. ADELAIDE STEAMSHIP CO LTD

- . High Court discarded the principle of general State immunity from Commonwealth legislation.
- . This case dealt with the power of the Commonwealth Arbitration Court to determine the wages and conditions of employees of State Governments. The High Court ruling extended the scope of Commonwealth power to State industrial activities, but its effects were much wider.

1926 PETROL TAX CASE (COMMONWEALTH V. SOUTH AUSTRALIA)

- . The High Court ruled that a South Australian tax of 2.5 cents per gallon on sellers of petrol was invalid, despite the fact that some of the petrol came from overseas, some from Victoria and some was produced within South Australia. The tax was ruled invalid under Section 92 (free interstate trade) and Section 90 (prohibition on States levying customs and excise duty) of the Constitution.

1927 NEWSPAPER CASE

(JOHN FAIRFAX AND SONS LTD V. NEW SOUTH WALES)

- . The High Court ruled that a New South Wales tax on newspapers published and sold in that State was invalid, on the grounds that it was an excise duty.
- . The Petrol Case and Newspaper case effectively excluded States from levying any tax on commodities.

1937 A.G. (NSW) V. HOMEBUSH FLOUR MILLS LTD.

- . High court ruling widens excise duty definition to cover any tax imposed in substance on production.
- . The case involved State legislation which expropriated flour, paid the former owner of the flour compensation and entitled the former owner to buy back the flour at a higher price. This was held to impose a tax measured by the difference between the compensation and repurchase price.

1938 MATHEWS V. CHICORY MARKETING BOARD

- . The High Court ruled that a levy of \$2 per half acre on land planted with chicory was invalid.
- . This case established the principle that a tax did not have to be specifically imposed on the quantity or value of goods produced to be an excise. It was sufficient for a tax to be imposed with respect to a commodity to be termed an excise.

1942 STATE OF SOUTH AUSTRALIA AND OTHERS V. COMMONWEALTH OF AUSTRALIA (FIRST UNIFORM TAX CASE)

- . The Commonwealth in 1942 introduced legislation which replaced separate State and federal income taxes with one single uniform national income tax. The legislation also provided for grants to be paid to States which abstained from levying income tax.
- . Victoria, Queensland, South Australia and Western Australia unsuccessfully challenged the legislation as unconstitutional.

1949 PARTON V. MILK BOARD (VIC)

- . A levy of 0.1 cents per gallon imposed by the Victorian Milk Board on sellers of milk who were not the original producers was declared to be an excise and therefore invalid.
- . Hence, a tax on a commodity at any point in the course of distribution was held to be an excise duty.
- . However, the High Court held that a tax on consumers or consumption cannot be an excise.

1957 VICTORIA V. COMMONWEALTH (SECOND UNIFORM TAX CASE)

- . The Victorian Government in 1955 took out a writ in the High Court challenging two aspects of the uniform tax legislation (New South Wales intervened in 1956 to support Victoria):
 1. Tax reimbursement grants being conditional upon the States not levying income taxes or reducing the grant payable if such actions were undertaken by the States. The challenge was unsuccessful with the High Court in 1957 upholding the validity of this aspect of the uniform tax legislation.
 2. Taxpayer's obligation to discharge any liability for Commonwealth income tax before paying State income tax. This challenge was successful with the High Court declaring in 1957 that this facet of the uniform tax legislation was invalid.

1958 DENNIS HOTELS V. VICTORIA

- . The validity of Victoria's liquor licence fees was challenged when they were increased in 1958.
- . The High Court ruled that:
 1. The annual licence fee based on sales during the previous twelve months was valid; and
 2. The temporary licence fee based on sales during the permit's duration was invalid.
- . This case formed the basis for State franchise fees based on sales in a previous period.

1963 BOLTON V. MADSEN

- . The High Court endorsed State taxes on road haulage.

1964 ANDERSON'S PTY LTD V. VICTORIA

- . The High Court endorsed State taxes on the provision of credit to finance purchase of goods. The case involved stamp duty on hire purchase and instalment sale agreements.

1969 THE STATE OF WESTERN AUSTRALIA V. HAMERSLEY IRON PTY LTD

- . In 1967 Western Australia introduced a requirement for a receipt to be issued for any payment valued at \$10 or more. Receipts were subject to stamp duty at the rate of 0.1%. All States copied this tax. Effectively, this was a tax on turnover.
- . The High Court ruled that the stamp duty on receipts of iron ore sales was an excise and therefore invalid under Section 90 of the Constitution.

DEC 1969-FEB 1970

THE STATE OF WESTERN AUSTRALIA V. CHAMBERLAIN INDUSTRIES PTY LTD

- . The High Court ruled that stamp duties on receipts in respect of sales at any stage from manufacture to consumption of goods manufactured in Australia were excise duties.
- . This did not invalidate stamp duty on receipts of wages and salaries (which was deemed to be a tax on services), although the States subsequently abandoned this duty altogether.

1971 VICTORIA V. COMMONWEALTH (PAYROLL TAX CASE)

- . The High Court held that the Commonwealth Parliament could legislate to impose a tax on State Governments by reference to the amount of wages paid by each State to its employees.
- . This was later relevant to the Commonwealth's imposition of fringe benefits tax on States.

1974 DICKENSON'S ARCADE PTY LTD V. TASMANIA

- . In 1973 the Tasmanian Government introduced a consumption tax on tobacco collected by tobacco retailers, accompanied by a business franchise fee on tobacco. The High Court considered that the collection of the consumption tax by tobacco retailers converted it from a consumption tax to a sales tax and therefore an excise duty. Hence the tax was ruled invalid.

- . However, the High Court upheld tobacco franchise fees, as it had upheld liquor franchise fees in the Dennis Hotels case.

1974 MG KAILIS PTY LTD V. WESTERN AUSTRALIA

- . The High Court disallowed a "licence fee" tax on the processing of fish.

1977 LOGAN DOWNS PTY LTD V. QUEENSLAND

- . States were excluded from imposing taxes on livestock used for the production of meat and wool.

1977 HC SLEIGH V. SOUTH AUSTRALIA

- . The High Court upheld fuel franchise fees, following its earlier decisions on tobacco and liquor licence fees.

1983 HEMATITE PETROLEUM PTY LTD V. VICTORIA

- . The High Court held that an annual licence fee imposed on the operator of pipelines was a tax on the production of the oil and gas carried by the pipelines and so an excise duty.

1985 GOSFORD MEATS PTY LTD V. NEW SOUTH WALES

- . The High Court disallowed an annual licence fee on the operator of an abattoir, as being a tax on the production of meat and therefore an excise duty (invalid under Section 90).

**1993 CAPITAL DUPLICATORS PTY LTD V
AUSTRALIAN CAPITAL TERRITORY.**

. The High Court held that a licence fee imposed by the ACT on the sale of videos by Capital Duplicators was an excise and therefore invalid.

. The High Court upheld its earlier decisions on the validity of tobacco and liquor licence fees (Dennis Hotels and Dickenson's Arcade) but expressed less support for fuel licence fees (which had previously been endorsed by the HC Sleigh case).

STATE - COMMONWEALTH FINANCES

There have been a number of important episodes in State-Commonwealth relations which have contributed to the loss of State independence since federation. The more important of these episodes are listed below.

SURPLUS REVENUE ACT 1908 AND THE BRADDON CLAUSE

The Constitution bound the Commonwealth to pay back to the States any revenue it raised over and above what was needed to meet its Constitutional responsibilities.

Under the so-called "Braddon Clause" and "book-keeping" arrangements, which determined how payments were to be made to the States in the first 10 years after federation, the Commonwealth was required to return to the States at least three quarters of all customs and excise duties to the States.

In 1908, however, the Commonwealth passed the Surplus Revenue Act which allowed it to avoid its obligation to pay the surplus to the States and keep more revenue for its own purposes.

This was an early move by the Commonwealth to expand its spending beyond its Constitutional responsibilities.

SURPLUS REVENUE ACT 1910

Following an agreement with the States the Surplus Revenue Act 1910 was passed, determining how payments were to be made to the States from 1910 to 1920 (the Braddon Clause and book-keeping arrangements ceased in 1910).

The Act provided for agreed per capita payments to the States of a smaller size than those made in the first 10 years. This was possible because by 1910 most States were in a sound financial position. Apart from Section 90, they had unlimited access to taxation revenues and most States had an income tax. There was no Commonwealth income tax.

Even then, special payments were to be made to the smaller States.

FEDERAL LABOR GOVERNMENT (1910-13)

Significantly increased Commonwealth expenditure into new areas.

WORLD WAR I AND THE COMMONWEALTH INCOME TAX

This period saw a large increase in Commonwealth control over the economy, commerce and trade (including many new taxes) and social services.

The Commonwealth introduced its own income tax in 1915 (the initially low rates increased by 25% in 1916-17 and a further 10% in 1917-18). Commonwealth income taxes existed side by side with State income taxes.

THE 1920s

During most of this period the Commonwealth Parliament was controlled by the Nationalist and Country Parties, who made a concerted effort to reverse the growth in Commonwealth power.

Negotiations were held to seek reductions in grants to the States and allow the Commonwealth to withdraw from the income tax field.

FINANCIAL AGREEMENT OF 1927

Established the Loan Council to coordinate and control all Commonwealth and State borrowings and established general coordination between the States and Commonwealth over public borrowing, debt repayment matters and grants to the States.

**COMMONWEALTH GRANTS COMMISSION
ESTABLISHED IN 1933**

The Grants Commission was established to formalise the payment of general revenue grants to the States after many years of dissatisfaction with the ad-hoc grant system since federation (mainly on behalf of the smaller States).

**WORLD WAR II AND INCREASING
COMMONWEALTH FISCAL DOMINATION**

This period saw the Commonwealth's financial dominance expand considerably.

Two key events were a large escalation in the Commonwealth's role in welfare services (ie. income redistribution) and, in 1942, the exclusion of the States from the income tax field and a large increase in income tax rates.

Following the War the States requested that they be allowed to re-enter the income tax field but this was not agreed to and several High Court challenges by the States were unsuccessful. The general revenue grants introduced by the Commonwealth to compensate the States for the loss of income taxes have continued to this day.

The Commonwealth's move to take the income tax power away from the States was a watershed in State-Commonwealth relations. In conjunction with the States being locked out of the sales tax field by the High Court's interpretation of Section 90, it has been instrumental in leading to the high degree of State dependence on the Commonwealth that we see today.

Exclusive income tax powers also gave the Commonwealth the fiscal capacity to support the steady increase in tied grants to the States and expand its expenditure into welfare services and undertake income redistribution.