

CHAPTER 5 – ECONOMIC REFORM AGENDA

Effective economic management has enabled the Victorian economy to achieve strong growth and weather the challenges presented by local and global uncertainties.

The government's objective is to maintain Victoria's economic growth by:

- continued investment and reform in key areas, including skills, infrastructure and business competitiveness;
- advocating national reform to boost economic growth in all states; and
- taking action to meet challenges to economic growth, including those presented by climate change and water supply constraints.

Council of Australian Governments (COAG) processes present the opportunity to achieve key national reform goals previously advocated by Victoria as part of the National Reform Agenda, including:

- a more effective framework for Commonwealth – State financial relationships, including wide-ranging reform to increase the flexibility and reduce the administrative cost of specific purpose payments, and the introduction of incentive payments to drive reforms of national importance; and
- better policy outcomes in areas of shared interest leading to stronger growth outcomes.

Victoria has enjoyed strong economic growth over the last decade, supported by continuing population growth, productivity growth and a rising participation rate. Looking ahead, Victoria faces a number of challenges to economic prosperity, including an ageing population, slowing productivity growth, changing global fortunes and environmental issues. These challenges highlight the importance of getting the most from Victoria's potential sources of growth – especially productivity growth and workforce participation – by continuing an active program of Victorian and national reform.

Victoria's reform program is designed to foster economic growth by:

- improving workforce participation and productivity by improving people's skills;
- investing in preventative health measures to provide for a healthy workforce;
- improving business competitiveness; and
- continuing to improve the quality and timely provision of infrastructure.

Policies are also aimed at meeting challenges to economic growth by:

- responding to climate change; and
- ensuring water security.

Victoria continues to pursue a program of state-based reform. In many areas, however, the shared objectives and overlapping responsibilities of governments, and the imbalance between their spending and taxing powers, makes collaboration between the Commonwealth and state governments essential to significant reform. The Victorian Government has consistently advocated such action.

COAG includes first ministers and treasurers from the Commonwealth and all states and territories and will meet quarterly, throughout 2008, to develop an ambitious program in key reform areas. These include health and ageing, the productivity agenda (including education, skills, training and early childhood development), climate change and water, infrastructure (including transport), business regulation and competition, housing and indigenous reform and, through treasurers, Commonwealth-State financial relations. Intergovernmental working groups have been established to oversee reform in each of these areas.

Forward work programs for these groups were agreed at the March 2008 meeting of COAG. This meeting also marked significant achievements in selected reform areas, with governments agreeing to a single governance framework for the Murray Darling Basin, additional funding for public hospitals, a national registration and accreditation system for health professionals, an accelerated regulation reform agenda and a program for expanded competition reforms. COAG also substantially reshaped Commonwealth – State financial relationships through the reform of specific purpose payment arrangements. Importantly, COAG agreed to the provision of new National Partnership reform payments to facilitate and provide incentives for governments to undertake wide ranging reforms in areas of joint responsibility, having regard to the economic benefits of proposed reforms.

Victoria's reform agenda includes areas of responsibility shared with the Commonwealth but there are also areas where Victoria is taking action alone, or leading activity in intergovernmental forums. The main reform areas are discussed in more detail below.

FOSTERING ECONOMIC GROWTH

Improving business competitiveness

Continued reduction of business costs, including tax changes, reductions in red tape, improvements to infrastructure and an emphasis on innovation and research and development will improve the national and international competitiveness of all Victorian businesses and help foster economic growth.

In July 2006, the government announced the *Reducing the Regulatory Burden* initiative, Victoria's policy for reducing the cost of regulation for businesses and not-for-profit organisations. The government announced that it would:

- cut the existing administrative burden of regulation by 15 per cent over three years and 25 per cent over five years;
- ensure the administrative burden of any new regulation is met by an offsetting simplification in the same or related area; and
- undertake a program of reviews to identify the necessary actions to reduce compliance burdens.

In terms of administrative burden, this translates into a net reduction equivalent to savings to business and not-for-profit organisations of \$154 million a year by July 2009 and \$256 million a year by July 2011. The productivity boost from reducing red tape has the potential to expand Victoria's economy by up to \$747 million a year (in 2005-06 prices) by 2016.

All departments now have three-year administrative burden reduction plans in place. Provisional estimates indicate that Victoria is on track to meet the July 2009 target. A detailed update on further prospective reductions as a result of changes implemented during 2007-08 will be released later in the year.

For example, implementation of the Victorian Government's food regulation reforms, in response to an inquiry undertaken by the Victorian Competition and Efficiency Commission, will deliver an estimated \$20 million a year in administrative savings to business and not-for-profit organisations.

Reviews have also commenced to deliver on the government's commitment to reduce the number of principal Acts of Parliament by 20 per cent by 2010. A total of 70 Acts have been repealed to date, and further repeal bills will be introduced for consideration by the Victorian Parliament during 2008.

Victoria is at the forefront of ongoing multi-jurisdictional action to reduce the burden of regulation. Victoria has taken a leading role in discussions within COAG, the Council for the Australian Federation, numerous Ministerial Councils, and bilaterally with other states, aimed at increasing harmonisation in regulatory definitions and administration, and minimising the cost of regulation to businesses, not-for-profit organisations, and individuals.

For example, New South Wales and Victoria have harmonised payroll tax legislation, including common definitions and exemptions, that will reduce payroll tax paperwork for around 8 000 businesses with operations on both sides of the Murray River. All jurisdictions have committed to joining the Victorian/New South Wales model as soon as practicable, with Queensland and Tasmania due to do so from 1 July 2008.

COAG's Business Regulation and Competition Working Group, established in December 2007, will drive the agreed COAG agenda for reduction of the regulatory burden on business by accelerating and broadening regulation and competition policy reforms and improving processes for regulation making and review.

At its meeting on 26 March 2008, COAG endorsed an accelerated reform agenda covering 27 existing and new areas of regulatory reform, in which harmonisation of occupational health and safety legislation is the top priority. An intergovernmental agreement on occupational health and safety harmonisation will be finalised by May 2008 and COAG will consider an accelerated implementation timetable in July 2008.

Infrastructure investment

Victoria faces a number of challenges in the effective management of its existing infrastructure assets as well as the planning and construction of new assets needed to support the state's ongoing economic growth and productivity. The government has recognised this through a significant investment program where almost \$30 billion will be spent over the next four years alone on infrastructure projects across the state. The government is investing heavily in social infrastructure, including modernising hospitals and schools, as well as economic infrastructure such as roads, rail lines and port facilities.

The 2006 Census of Population and Housing has highlighted the challenges facing Victoria from higher than anticipated population growth, especially for metropolitan Melbourne. This is expected to continue and requires careful planning and timely decisions about Victoria's infrastructure needs over the next 20 years. Other demographic challenges facing the state include the ageing population, changes in household composition and population movements across Victoria, all of which need to be considered in determining infrastructure requirements.

The government is currently making a number of significant investments to improve the efficiency of the freight transport network. Deepening the shipping channels of Port Phillip Bay will allow the Port of Melbourne to accommodate the global trend towards larger container ships. This will assist Melbourne to remain the leading container port in Australia.

The government commissioned the *East West Link Needs Assessment* to develop options to address future demands on transport connections across Melbourne's east-west corridor given the expected growth in freight and passenger movements. The advice prepared by Sir Rod Eddington was publicly released in April 2008 and submissions on its findings have been invited. Public comment will inform government decision making on future transport links in metropolitan Melbourne.

An example of this government's commitment to social infrastructure is a long-term program of rebuilding or modernising every Victorian government school over a 10 year period. The *Victorian Schools Plan* will transform education infrastructure by ensuring all Victorian government schools are equipped to provide high quality education to their students.

A number of new schools are being developed under the program through public-private partnerships, which offer an opportunity to combine the skills of the public and private sectors. The private sector is responsible for the design and construction of the new school facilities and the ongoing asset condition and performance over the life of the buildings, while the state retains responsibility for the delivery of all core education and curriculum services.

More broadly, the COAG process presents a new opportunity to tackle the infrastructure investment challenges across jurisdictions. Efficiency gains will be accrued through collaborative action to streamline planning processes, removal of regulatory duplication and the creation of a national market to facilitate infrastructure investment and construction. The first step in this process involves an assessment of the adequacy of the nation's economic infrastructure to inform future funding decisions for infrastructure projects that are agreed national priorities. Victoria has called on the Commonwealth Government to increase its funding contribution to meeting national infrastructure requirements.

Increasing skill levels

The education and skills of Victoria's population are strong influences on both the prosperity of the state, and the opportunities of individuals.

Labour force and productivity growth are the key determinants of Victoria's long-run economic growth, and thus the prosperity of the state. Over the coming decades, an ageing population means that economic reform will need to deliver higher labour force participation and stronger productivity growth if Victoria's prosperity is to be sustained.

The knowledge and skills of Victoria's workforce influence both labour force participation and productivity. Those with higher skills are more likely to participate in the workforce and to work to an older age. They are also more productive and innovative, and better able to adapt and contribute to changing circumstances.

Higher levels of education deliver a range of lifetime benefits to individuals, including higher incomes, lower rates of unemployment and better health and wellbeing. Reforms that improve education outcomes and encourage more people to stay in or re-enter education and training therefore also have important implications for equity, helping to improve the distribution of the benefits of economic growth.

Vocational education and training

The Victorian vocational education and training (VET) system has undergone significant reform over the past two decades, through the introduction of a nationally unified training system and substantial reforms driven at the state level. As a result, the Victorian public training system is the most devolved in the country and Victorian Technical and Further Education (TAFE) institutions lead against most national benchmarks.

However, Victoria faces a number of challenges to its future economic prosperity: increased global competition; slowing productivity growth; an ageing population; and intensifying skill shortages.

Challenges within the current training system also have to be overcome to ensure the right mix of skilled workers. The Centre for the Economics of Education and Training has projected that stronger demand for higher level skills will require a change in the mix of training – away from lower level qualifications and towards diplomas, advanced diplomas and higher level certificate courses – if the state’s skill requirements are to be met.

Further reform is also needed to make the system more outward looking and responsive, and to improve its ability to address skill shortages.

The Victorian Government has recently released a discussion paper which proposes ambitious reforms in response to these challenges. The reforms are designed to achieve four objectives:

- boosting numbers of individuals and businesses accessing training, which will increase the skills of Victoria’s workforce;
- developing a VET system that engages more effectively with individuals and businesses and is easier to navigate;
- ensuring the system is more responsive and flexible to the changing skill needs of businesses and individuals; and
- creating a stronger culture of lifelong learning.

The proposed reforms include:

- increasing access for eligible Victorians to a government supported training place and increasing investment from those who benefit most from training: government, businesses and individuals;
- strengthening the capacity of the TAFE and Adult, Community and Further Education sectors;
- improving choice and contestability by enabling individuals and businesses to access government supported training at a broader range of public, private and community providers; and
- improving information to make it easier for individuals and businesses to understand and use the training system.

COAG has also endorsed goals that reflect the need to broaden and deepen the skills of the working age population and improve the match between the supply of skills and changing labour market demands.

Schools and early childhood

The essential building blocks for lifelong learning and skill building are established in early childhood and at school.

These are areas where Victoria already performs well by national and international standards, but continuing reform will be needed to ensure that Victorian children keep pace with the best in the world.

Future reform priorities include continued improvement in the quality and reach of early childhood education services and the quality of teaching, supported by strong accountability systems, and more accessible and comprehensive information for parents.

The recent establishment of the Department of Education and Early Childhood Development has provided an opportunity to improve and integrate early childhood services and schools across Victoria. The government is developing a *Blueprint for Early Childhood Development and School Reform*, with community input, that builds on earlier reforms to establish integrated strategic directions, actions and targets for the education of Victorian children from birth.

The *Blueprint's* proposed five-year reform agenda aims to improve educational health and wellbeing outcomes, provide an accessible high-quality service system for early childhood and schools, and reduce the effects of disadvantage on children and young people's learning and development. The *Blueprint* will include a range of actions to enhance partnerships with parents and communities, strengthen system development and design, and build workforce capacity. Key actions proposed for the *Blueprint* include:

- engaging families of children of all ages and providing guidance on supporting learning and development;
- developing schools as community hubs through better cross-sectoral planning, co-locating of services and more community use of school facilities;
- building greater continuity in the approach to the learning and development of children up to eight years old and improving transitions to school;
- publishing information on provider performance and broadening parental choice; and
- improving coordination, professional development and use of non-teaching staff.

At the national level, all governments have agreed for the first time on a common framework for reform of education, including a comprehensive set of aspirations, outcomes, progress measures and future policy directions.

COAG has also agreed to the development of a National Partnership agreement focused on the particular educational needs of low socioeconomic status school communities. This partnership will form part of the national education funding agreement to be introduced at the beginning of 2009.

A healthy workforce

In addition to being better for the lives of Victorians, improving the health of the population is essential to maintaining Victoria's economic growth.

Dealing with the rise of chronic disease remains a particular challenge for government, and one where the pay-off of effective reform to improve prevention is likely to be substantial. Chronic diseases account for a large proportion of Victoria's health spending and have a high cost in terms of lower workforce participation and reduced productivity. Cancer is the leading cause of death in Victoria, with around 500 Victorians diagnosed with cancer every week. Mental illness imposes significant costs, totalling over \$5 billion a year in Victoria through both direct costs and the costs associated with reduced workforce participation and productivity. Type 2 Diabetes accounts for 1.6 per cent of total health system expenditure in Australia.

The government is committed to a coordinated approach to improving prevention of chronic disease, and recent initiatives are designed to begin reducing the incidence of the most common diseases.

For example, income from a \$600 million fund to be set aside from *WorkSafe's* surplus funds will provide funding for a new *WorkHealth* initiative to target the connection between chronic disease and workplace injury by providing information, advice and work-place screening to assess workers at risk of developing chronic diseases such as diabetes and heart disease.

This budget commits \$150 million over four years to the *Victoria's Cancer Plan 2008-2011* initiative which will focus on improving survival rates and build on innovation in early diagnosis, prevention, treatment and research. A key element of this initiative is funding for the Victorian Cancer Agency and Victorian Cancer Biobank, to ensure that cancer care is informed by the latest technology and research.

The development of a Victorian mental health strategy aims to provide a comprehensive systemic response to mental health for the whole population, with a focus on awareness promotion and prevention. The 2008-09 Budget commits around \$77 million over four years and \$34 million in capital funding to improving mental health services and facilities.

Although the focus on prevention is increasing, it is clear that much more effort will be required in coming years, including at a national level. A key priority of the newly established COAG Health and Ageing Working Group is enhancing the fitness and health of Australians through improved primary prevention.

This work will need to be informed by a strong evidence base that identifies effective interventions. The long-term campaign to cut smoking rates in the community may provide models for dealing with other risk factors and chronic diseases. Further work in this area will require the efforts not just of Victoria, but also other states and territories and the Commonwealth, to turn local health promotion and preventative initiatives and ideas into proven and well supported programs.

MEETING CHALLENGES TO ECONOMIC GROWTH

Responding to climate change and water

Over coming decades, climate change will create a number of economic challenges for Victoria. For example:

- as rainfall declines and becomes more variable, there will be more pressure on water supplies and primary production, with consequent cost impacts;
- more extreme weather events and possible sea level rise will increase risks to infrastructure assets, coastal settlements and tourism; and
- mitigating greenhouse gas emissions through the introduction of an emissions trading scheme will put more pressure on energy costs, with impacts on both industry and households.

The Victorian Government began a process of public consultation on 4 April 2008, with the Climate Change Summit and the release of the summit paper, *A Climate of Opportunity*. This is to be followed by a Green Paper, and finally a White Paper setting out a climate change policy framework for Victoria.

Governments in general will need to act in three broad areas: measures to mitigate climate change by reducing emissions, adaptation to the effects of unavoidable climate change and assisting with the necessary structural adjustment to a low carbon economy. Governments face the challenge of setting a policy environment that enables emissions abatement to occur at least cost and facilitates adaptation to the unavoidable impacts of climate change.

Mitigation

The challenge of addressing climate change is significant, but not incompatible with continued strong economic growth. Economic modelling from a range of sources, such as the Stern Review of the economics of climate change, the States and Territories' National Emissions Trading Taskforce, the Australian Bureau of Agricultural and Resource Economics, and the recent Garnaut review draw similar conclusions, namely that with efficient policy responses, even substantial cuts in emissions should have only a modest impact on economic growth over the longer term.

The key to reducing emissions with minimal impact on living standards will be the use of market-based instruments to target least-cost emissions abatement. A national emissions trading scheme will form the centrepiece of the mitigation effort. However, because emissions prices are likely to ramp up over time, at least in the early years an emissions trading scheme alone may not drive abatement at lowest cost. Complementary policies will need to be considered to target other market failures such as lack of information about energy efficiency opportunities, or under-incentives to invest in research and development.

Commonwealth, state and territory governments will each have a part to play in the delivery of these complementary measures. In October 2007 the Victorian Government announced the *Victorian Energy Efficiency Target* scheme, a market-based measure that will encourage households to increase their energy efficiency, cutting greenhouse emissions and utilities bills. Innovation in the energy sector is being driven by the Energy Technology Innovation Strategy, which supports accelerated development of low-emission energy technologies such as clean coal and large-scale solar power that will be essential to future abatement.

The introduction of a carbon price at the national level will necessarily drive up energy costs, particularly affecting low-income households who are constrained in their ability to adapt to rising prices. As with complementary measures, Commonwealth, state and territory governments will have a role to play in addressing these impacts. Victoria has a generous concession program targeting concession card holders with the aim of increasing affordability of household utilities. However, the Commonwealth administered tax-transfer system is the best mechanism for addressing the impact of increased energy prices on low income households in the future.

Adaptation

Regardless of efforts to reduce greenhouse gas emissions, some degree of climate change now appears inevitable. Over 2008, Victoria will work with other jurisdictions through COAG to review the *National Climate Change Adaptation Framework* and develop an implementation plan. The revised Framework will include possible actions to assist the most vulnerable sectors and regions to adapt to the impacts of climate change.

Climate change will bring challenges and opportunities for the agriculture industry. Farmers' ability to manage climate change risks will be central to reducing their vulnerability to the new climate and remaining competitive. In addition, structural adjustment will become more rapid. State and Commonwealth government agricultural policies will need to work in synergy and actively facilitate structural adjustment.

To support the agriculture sector through this change, the Victorian Government has reshaped and strengthened its services and policies to assist farm businesses and rural communities to meet the challenges ahead and capture new opportunities. The *Future Farming* strategy, recently announced by the Premier and the Minister for Agriculture, will assist farmers to build competitive and productive businesses that are sustainable in the face of unprecedented change. Victoria will seek similar change in Commonwealth Government policy, including through input into the Commonwealth review of Exceptional Circumstances assistance.

Managing risks from climate change

Climate change will create new risks and opportunities and will also increase risks associated with, for example, more frequent and intense droughts, floods and bushfires. Government has a role in providing information on climate related risks. However, where there are private benefits from doing so, business and individuals are best placed to take reasonable steps to manage their exposure to climate-related risks.

The Victorian Government will give particular emphasis to protecting public assets, building knowledge and sharing information about climate change impacts, raising awareness of adaptation options and discouraging unnecessary risk taking. The Victorian Government has already commenced this work, commissioning climate change impact assessments for Victoria's infrastructure assets and conducting regional level climate change projections and regional pilots to raise awareness and encourage the development of adaptation action plans.

While individuals and businesses are best placed to manage their own exposure to climate change risks, there may be instances where these risks are beyond the capacity of the community to manage.

Water security and flexibility

With climate change expected to bring greater uncertainty about future rainfall patterns, Victoria is investing in diverse and flexible strategies to manage the state's water supply, and ensure the security of supply at least cost to society.

Urban water reform

Our Water Our Future, The Next Stage of the Government's Water Plan, identifies \$4.9 billion in projects to diversify and secure water supplies in the long term. The creation of alternative sources of bulk water supply (along with greater interconnection) presents new opportunities to provide a more modern, dynamic and efficient water supply system for the future.

To inform the government on such system reform, in 2007 the government directed the Victorian Competition and Efficiency Commission (VCEC) to carry out a review for improving the structure of the metropolitan retail water sector. The government also asked the Essential Services Commission (ESC) to review water tariff structures to complement the VCEC review. The government response to the VCEC review is to be released by no later than August 2008.

Rural water reform

Ongoing reform of rural water management in Victoria has helped to prepare the state's regional communities for climate change. In July 2007 irrigation water rights were unbundled from land titles, creating a water share (defining an irrigator's entitlement to a share of water), a delivery share (giving irrigators an entitlement to have water delivered to their property) and a water use licence (defining an irrigator's authority to use water for irrigation on their property). Unbundling has also enabled termination fees to replace exit fees, so that when irrigators sell water entitlements they can choose to retain their delivery share (and pay fixed charges associated with that share) or pay a termination fee. This flexibility minimises barriers to trade whilst ensuring appropriate cost-recovery for existing infrastructure. The Water Register, which went live on 1 July 2007, also stimulates the expansion of water trade and should in future ensure reliable and streamlined approval processes for intra and interstate water trading.

The opening up of Victoria's water trading system has helped to lessen the burden of the recent long drought by providing a mechanism to manage risk. Buyers and sellers can trade either permanent entitlements or seasonal allocations depending upon their individual needs and preferences.

While the net value created by trade is overwhelmingly positive, the impacts of trade are complex and vary across regions. The resulting structural adjustment will need to be managed without unduly constraining opportunities for trade, since trade itself provides an important adjustment mechanism.

The very substantial program now underway in northern Victoria to modernise ageing irrigation infrastructure is expected to generate an estimated 225 gigalitres (GL) of water savings, to be split three ways between irrigators, Melbourne and the environment and will provide further opportunities for reform.

The Memorandum of Understanding for Murray Darling Basin reform, signed at the March 2008 COAG meeting, was a major step forward, with the Commonwealth agreeing to Victoria's proposals with respect to Basin governance and appropriate protections for existing property rights. Victoria has long advocated reform of water management arrangements in the Murray Darling Basin, including giving the Commonwealth greater power to set and enforce sustainable diversion limits, and to enforce market rules that ensure a level playing field in interstate water markets.

In addition, Victoria and the Commonwealth have agreed on a plan for water security in the Murray Darling Basin, which will provide for further modernisation works in the Northern Victorian region. This is expected to generate a further 200 GL in water savings to be split equally between irrigators in the region and the environment. A key issue for reform into the future through the COAG process is investigation into the most appropriate measures to facilitate structural adjustment in water intensive industries and communities.

The health of Victoria's rivers and water ways is also under stress under the current climatic conditions. Encouraging private investment and using market mechanisms, including water trading and tenders, in both regulated and non-regulated rivers, can be an efficient and effective means of recovering water for the environment.

Water markets present opportunities for water to be allocated to its highest value use. This increases efficiency in the urban and rural sectors and for accessing environmental water. Combining this with a diverse and flexible water supply will best equip Victoria for the uncertain climatic years ahead.

REFORM TO COMMONWEALTH-STATE FINANCIAL RELATIONS

Reform of Commonwealth-State financial structures, including improved efficiency and accountability, provides an opportunity to support increased economic growth in Victoria. The need for this reform is heightened by Australia's relatively high degree of vertical fiscal imbalance and the significant degree of overlap in responsibilities between levels of government.

Vertical fiscal imbalance reflects the mismatch between the spending responsibilities and revenue raising capacities of governments. States are responsible for providing the majority of core services – in areas such as health, education, transport and law and order – while the Commonwealth has primary capacity to raise revenue (through taxation) to fund them.

This imbalance has grown with High Court rulings on the unconstitutionality of state franchise fees and the abolition of state taxes (in return for the receipt of Goods and Services Tax (GST) revenue) under the *Intergovernmental Agreement on Reform of Commonwealth – State Financial Relations*. Grants from the Commonwealth have grown from less than 40 per cent of Victoria’s revenue in 1996-97 (when franchise fees were removed) to 46 per cent in 2008-09. Victoria, like other states, is now increasingly reliant on funding from the Commonwealth to provide core services. This challenge is compounded by the fact that Victoria receives significantly less than its population share of Commonwealth grants.

Victoria currently receives two main types of Commonwealth grants: specific purpose payments (SPPs) and GST revenue. These are detailed in Budget Paper No. 4, Chapter 4, *State Revenue*. In early 2008, COAG agreed to undertake major reform of SPPs creating a new architecture for Commonwealth-State funding. Governments have also continued to work on the 2010 Commonwealth Grants Commission (CGC) review of methodology for distributing GST revenue, pursuing a simpler, more transparent and more efficient system.

Specific Purpose Payments

SPPs include payments ‘to’ the states, retained by state governments for their own use, and payments ‘through’ the states, which are passed on to other bodies and individuals on behalf of the Commonwealth. Total SPPs (including those for on-passing) account for around 40 per cent of Commonwealth funding to Victoria, and around 20 per cent of Victoria’s total revenue.

SPPs provide essential contributions to funding for state services, including health, education, housing, roads and community welfare. They are also an important vehicle through which governments can develop agreed objectives and reform priorities in areas of shared responsibility. For this reason, Victoria, along with other states, has sought for many years to have the design of SPPs reflect the flexible and efficient environment necessary to maximise achievement of real outcomes.

In March 2008, COAG agreed to a new architecture for Commonwealth – State funding. Overall, this new architecture will provide a solid foundation for efficient delivery of core services and strengthened incentives for reform.

From January 2009, the large number of existing SPPs (around 90 grants nationally) will be restructured into two new funding streams: new generation SPPs and National Partnerships (NP).

Five or six new broad based, outcome focussed SPPs will be developed in the areas of health, education, skills, housing and community-disability services. These will be structured very differently from existing SPPs. Input controls – the prescriptive conditions which have constrained state flexibility in the past – will be removed and replaced by high level objectives to deliver agreed, shared outcomes. These ‘Statements of Objectives and Outcomes’ will be supported by new standardised accountability

frameworks, which focus on timely reporting to the community on outcomes and streamline the detailed and onerous reporting of administrative data. Rather than having fixed terms, these grants will be ongoing, with periodic review of outcomes and funding adequacy. New generation SPPs will provide states with greater ongoing financial certainty (in base funding and growth factors), give states the flexibility to deliver agreed outcomes in the most efficient and locally effective way, and remove the restrictions of detailed input based conditions and reporting.

A second form of funding, NP payments, will also be developed. These arrangements will be used where governments agree to undertake specific projects or reforms. NP reform payments may include payments to states to assist with the up-front costs of reform, as well as to reward states for progress and share the economic benefits of reform. Progress against reform milestones will be assessed by an independent body, and reward payments paid in line with achievement. This is similar to the National Competition Policy process and payments, which successfully drove a program of micro-economic reform in the mid 1990s. Where one-off projects or reform-based initiatives have proven ongoing benefits, these can then be rolled into the relevant broader SPP, providing a balance between the need to pilot specific new projects and approaches to broader funding flexibility.

Other existing SPPs will be variously terminated or cashed out, converted into untied or general revenue assistance or reclassified as Commonwealth own-purpose expenses.

Victoria strongly supports these reforms, which provide a solid architecture for Commonwealth-State funding arrangements. The challenge now facing governments is to agree to objectives, funding and accountability frameworks for each of the new grants. To fulfil the potential of progress achieved to date, these reforms must reflect a shared commitment to improved outcomes, with investment and risks allocated fairly across governments.

MAINTAINING THE MOMENTUM

Victoria has enjoyed strong economic growth and in order to sustain this growth into the future the government has invested in many sectors, including infrastructure, skills, improving business competitiveness and a healthy workforce, and further reform is in prospect in these areas. The government is also taking action to mitigate the risks to growth from climate change and to secure Victoria's water supplies.

At a national level, Victoria is working with the Commonwealth to improve Commonwealth-State funding arrangements and community outcomes in the areas of joint responsibility.

The government is taking action now to meet the challenges of the future, and has a clear plan for addressing ongoing reform priorities.

