

APPENDIX 1
INTERGOVERNMENTAL
RELATIONS IN FEDERAL
SYSTEMS

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1 | INTRODUCTION

Australia, like many other systems of government around the world, is a federal system. Federations, while divided into different levels of government inevitably have a degree of interdependency between governments. Inescapably there arises a degree of conflict or ineffective governance. For example, disputes may arise between different governments on the basis of service provision or infrastructure, constitutional jurisdiction, fiscal arrangements (e.g. vertical fiscal imbalance or spending powers) or environmental or social issues.

Most federations have developed a system of intergovernmental consultation and cooperation to deal with such issues, and to manage and foster cooperation between governments. The character of intergovernmental arrangements is unique to each federation, and depends on various factors such as history, geography, population, size and formal federal arrangements. While intergovernmental processes and arrangements are a common feature of federations around the world, the form of such arrangements varies depending on the specific circumstances of each federation.

Comparisons of intergovernmental arrangements of different federations can provide insights into how Australia's intergovernmental arrangements might be strengthened, and the pitfalls that might be faced if reform of intergovernmental arrangements is not achieved. Many federations are grappling with similar issues to those being faced in Australia and there are lessons to be learned from those countries.

Various issues need to be considered.

Firstly, should the intergovernmental arrangements be federal–state or interstate? In most federal systems, both forms are used. For example, Canada and Switzerland and more recently Australia, have recognised the need for interstate formal arrangements by establishing a forum for achieving consensus across sub-national governments on issues, including federal–state. On the other hand, most federations have some form of federal–state forum that deals with both vertical and horizontal collaboration. Such federal–state forums generally vary from federation to federation in the degree of institutionalisation and formality.

Secondly, a consideration of the degree of formality of intergovernmental arrangements is required. The types of forums that have been established across federations vary from formal (e.g. constitutional entrenchment) to informal (e.g. meetings called on an ad hoc basis). 'As Australia has illustrated, constitutionalization is not essential, but extra-constitutional formal councils do have an advantage over merely ad hoc bodies'.¹

In considering similar issues in Canada, one commentator stated:

... the intergovernmental institutions will need to be genuinely collaborative in character, rather than instruments for intergovernmental imposition. But provision for some formal institutions to improve intergovernmental collaboration and reduce friction and conflict in Canada would appear to be overdue. At the same time, in establishing formal institutions to improve intergovernmental collaboration it will be essential to ensure that they are open, transparent, accessible and responsive in order to avoid any public sense that they will contribute to a 'democratic deficit'.²

.....

Thirdly, consideration of forums that may not be linked to government or political persuasions may be required. What has hampered collaboration and outcomes in many federations has been a focus on political ‘jockeying’ and buck-passing rather than long-term perspectives. There may be some alternative systemic institutional arrangements that can be developed to achieve greater accountability, transparency and independence in policy setting initiatives. This would involve establishing an institution made up of individuals with policy expertise and who are not influenced by political views. This jointly funded federal–state body would be primarily dealing with issues relating to the federal system and be able to provide research and data on federalism and prepare reports on the state of the federation and other special issues as they arise.

Fourthly, consideration of appropriate accountability and transparency as well as collaboration that can be achieved from intergovernmental fiscal arrangements must also be a high priority. Policy making and the ability to implement decisions as well as accountability for policy making are inextricably linked; any consideration of intergovernmental arrangements cannot avoid consideration of fiscal arrangements. These arrangements differ across federal systems depending on the formal arrangements (e.g. constitutional as well as legal interpretation) as well as historical and other developments. While it may be difficult for Australia to emulate other jurisdictions in terms of fiscal arrangements (e.g. taxation arrangements are politically sensitive and difficult to alter) it may be worthwhile to highlight how Australia differs from other countries, and why this should be reviewed for long-term effectiveness.

The BCA has argued since 2005 that Australia needs a new national reform agenda, highlighting four key areas for reform: tax, infrastructure, regulation and workplace relations. Some of what the BCA sought in terms of specific reform actions was delivered when the Council of Australian Governments (COAG) agreed in February 2006 to a new reform agenda covering education, training, infrastructure and regulation.

These positive responses, however, have been reactions to specific problems and do not represent a holistic approach to issues that arise with Australia’s federal system. COAG needs to be driving the reform agenda that anticipates reform issues and positions Australia to be able to compete in the future in a global economy. This has led the Productivity Commission to comment:

Collective and cooperative action will be especially important in responding to future challenges – such as globalisation, environmental sustainability and population ageing – because of the extensive cross-jurisdictional elements associated with the challenge. The Commission has highlighted the need for national coordination in a number of key reform areas, including health, the environment and freight transport, and has emphasised the strong leadership role required from CoAG.³

Cooperation between governments in Australia is essential for facilitating a variety of reforms to improve Australia’s performance and productivity. Effective intergovernmental relations are necessary to reduce the overlap and duplication of regulation and service delivery and to facilitate decision making by different levels of government. They are ‘also necessary if the virtues of federalism are to be realised in Australia.’⁴ Accordingly, high-level leadership, as well as a systematic way of identifying, agreeing and implementing reforms (including refining and monitoring progress), is necessary.

2 | FEDERAL SYSTEMS

Federal systems consist of different levels of government, commonly a national or central government and a set of regional or sub-national governments (e.g. states in Australia, provinces in Canada, Länder in Germany and states in the United States).

What broadly distinguishes federal systems from unitary systems is that legislative power rests with the central government in a unitary system, but is divided and shared between the different levels of government in a federal system. The division of powers in a federal system is generally governed by a constitution. 'In a federal system of government, sovereignty is shared and powers divided between two or more levels of government each of which enjoys a direct relationship with the people.'⁵

Ronald Watts, former Principal of Queen's University, Kingston, Ontario and Fellow of the Institute of Intergovernmental Relations, provided a discussion of federations worldwide in his background paper, 'Federalism Today', presented at the International Conference on Federalism in August 2002:

Federalism provides a technique of constitutional organization that permits action by a shared government for certain common purposes, together with autonomous action by constituent units of government for purposes that relate to maintaining their distinctiveness, with each level directly responsible to its own electorate. Indeed, taking account of such examples as Canada, the United States and Mexico in North America, Brazil, Venezuela and Argentina in South America, Switzerland, Germany, Austria, Belgium and Spain in Europe, Russia in Europe and Asia, Australia, India, Pakistan and Malaysia in Asia, and Nigeria, Ethiopia, and South Africa in Africa, some 40 percent of the world's population today live in countries that can be considered or claim to be federal, and many of these federations are clearly multicultural or even multinational in their composition.⁶



3 | WHAT ARE INTERGOVERNMENTAL RELATIONS?

Intergovernmental relations are the responses that have been developed to facilitate cooperative policy making among divided governments within a federal system. Intergovernmental relations are supposed to play a 'bridge-building' role to bring a degree of coordination and cooperation to divided powers.

The federal systems of most countries have arisen because of the historical circumstances of those countries and commonly as a means of creating stability and union among a group of 'states' that have varying characteristics. The founders of those federal systems focused on formal constitutional rules and the division of powers between the states as a means of establishing a stable union. Most federal systems did not formally include the need for subconstitutional and informal arrangements for intergovernmental coordination and cooperation.⁷ In addition, many federal systems have built in mechanisms within their constitutions making it difficult to amend the constitution (and therefore the limitation has made it difficult for those countries to later incorporate formal constitutional intergovernmental arrangements into their constitutional arrangements). It has been common for modern federal systems to develop informal intergovernmental relations in response to their own unique federal circumstances:

Changing political, economic and social realities are less likely to be addressed by formal constitutional amendments. Instead, there is growing reliance on intergovernmental treaties or accords.⁸



4 | AUSTRALIA'S FEDERATION – HOW IS IT OPERATING?

Australia's federation has a number of distinctive features, including:

- + A comparatively high degree of shared functions between governments.
- + A strong centralising trend over time.
- + A relatively high degree of vertical fiscal imbalance (with transfers directed at fiscal equalisation).
- + Innovative initiatives in cooperative federalism (such as mutual recognition schemes, harmonisation schemes and national standards).⁹

The Australian Constitution creates a highly concurrent federal structure, which means that intergovernmental relations are very important for the system to operate effectively. The powers that are not specifically assigned to a level of government in the Australian constitution ('residual' powers) reside with the states. There are only a few 'exclusive' powers of the Commonwealth, and a broad set of 'concurrent' powers between federal and state (section 51 of the Constitution) with the federal jurisdiction having paramountcy where there is conflict. 'So the Constitution not only mandates overlapping powers, it also facilitates them ...'¹⁰

In addition, the states are highly financially dependent on the Commonwealth (vertical fiscal imbalance). This means that the Commonwealth has become involved in many areas of policy making that would otherwise be the responsibility of the states. This means that there is overlap (both vertical and horizontal) in the operations across governments. The distribution of authority, coupled with vertical fiscal imbalance, means that conflict is a feature of the management of the Australian system, and that the 'smooth functioning of a federation so concurrent in its structure is dependent upon effective intergovernmental relations.'¹¹

EXHIBIT 1

CONCURRENCY OF POWERS

Because there is a tendency to think about governments fulfilling 'functions', it would be easy to slip into thinking of this discussion as being about how functions will tend to be comparatively sorted – that is, divided. The reality is that all things that are appropriately categorised as policy functions – health, education, welfare, defence, law and order, labour markets, environment, agriculture and many more, involve collections of activities with quite different shaped cost functions and, correspondingly, different spheres of government are likely to have a comparative advantage in providing different activities, even allowing for the possible gains to them from coordination with other governments up or down the production chain. So for example, in welfare policy 'activities' range from setting tax and cash benefit structures through labour market training programs to the provision of public housing or of shelter for homeless persons.

Source: C Walsh, 'Competitive federalism – Wasteful or Welfare Enhancing?' Productivity Commission *Productive Reform in a Federal System*, Roundtable Proceedings, Canberra, 2006, p. 63.



Governments are the main agents of economic management and reform. They establish policy frameworks, settings and limitations that have a major influence on a nation's current and future prosperity. A critical part of their role is to anticipate and manage emerging economic challenges and opportunities that can affect the performance of Australia's economy.

Governments, as economic managers, should discharge three key responsibilities:

- + **Anticipating** possible or emerging economic barriers and opportunities – in a fast-moving, global environment, successful economies must anticipate emerging risks and opportunities and respond accordingly.
- + **Agreeing** on the reforms necessary to avoid the barriers and seize the opportunities – under a federal system, most solutions will require the agreement and commitment of more than one level of government.
- + **Implementing** the agreed solutions – successful implementation is most likely where the goals of reform, and the progress towards those goals, are transparent and governments are held to account for their performance.

While there may be benefits arising from the inherent competition in Australia's federal system, there must also be a mechanism to ensure efficiency. Detrimental effects such as overlap, duplication and disputes about responsibility must be avoided while achieving a long-term strategic vision for the future. The costs of overlap and duplication and inefficiencies in Australia's federal system are highlighted in the Access Economics report, *The Costs of Federalism* (Appendix 2), and estimated to be approximately \$9 billion. There are obvious economic advantages therefore to reducing the unnecessary costs and to ensuring a strategic, comprehensive, long-term strategy is established. How can this be done in the context of such interdependence and competition across governments?

To anticipate, agree and implement policy reform for the good of the economy, there is a strong need for intergovernmental cooperation in Australia. Through the Special Premiers' Conferences and COAG, among other initiatives, a number of cooperative arrangements as solutions to specific problems have been implemented in Australia since the 1990s. An example of a substantially successful initiative was the National Competition Policy (NCP) framework. However, although the success of those initiatives is commendable, a process to ensure that there is ongoing consideration of policy reform initiatives is essential.

Gary Banks, Chairman of the Productivity Commission, suggests that the success of the NCP reform process was attributable to:

- + Recognition by all governments of the need for reform.
- + Broad agreement on the priority areas.
- + A solid framework and information base to guide policy prescriptions.
- + Some highly effective procedural and institutional mechanisms to implement reform.¹²



Do similar frameworks exist to ensure successful initiatives such as NCP occur in the future in other areas (e.g. infrastructure, tax, regulation, health, education)?

Notwithstanding the improvement in Australia's economic performance in recent years, inefficiencies and performance gaps remain and will need to be addressed if Australia is to meet significant challenges ahead. Many of the areas offering the potential for significant benefits extend beyond the existing NCP reform agenda, but share in common the fact that coordinated national reform has a real and important role to play.¹³

What is required is a method of ensuring that the three objectives outlined above (anticipating, agreeing and implementing) can be met across the Australian economy – and that there is a shared vision for the operation of the Federation. Consideration should therefore be given to establishing systemic changes within Australia's federal structure to facilitate the identification of potential or emerging economic challenges and opportunities and appropriate responses to those. Intergovernmental institutions provide a stable framework for negotiations and a framework for effective decision making.

EXHIBIT 2

THE NECESSITY FOR POLITICAL LEADERSHIP AND REFORM

Many participants stressed the importance of cooperation between governments in facilitating a variety of reforms that could materially improve Australia's productivity and growth performance. In this context, several participants stressed the need for high level political leadership and dialogue for developing and refining reform initiatives and monitoring progress over time ...

Source: Productivity Commission, *Productive Reform in a Federal System*, Roundtable Proceedings, Canberra, 2006, p. 13.

There appear to be two main deficiencies in Australia's federal system that are causing inefficiencies, duplication, overlap as well as a lack of transparency and accountability of governments and their actions and short-termism in focus towards the operation of the federal system. These are:

- + A lack of adequate institutions for intergovernmental relations that will enable anticipation, agreement and implementation of agreed policy by governments.
- + A lack of appropriate funding arrangements to reduce inefficiencies in our federal system.

Under these two main topics, this study considers the experience of a number of other federal systems to ascertain whether there are lessons to be learned that could be applied or adapted to solve some of the emerging problems in Australia's federal system.

5 | INTERNATIONAL COMPARISONS

The Productivity Commission has noted that 'about 25 of the world's 193 countries have federal systems of governance, accounting for about 40 per cent of the world's population and about 50 per cent of global GDP.'¹⁴

Lessons can be learned from other federal countries and the way their systems of federation operate. Other federations may be adopting new and innovative approaches to creating an efficient federal system and fostering cooperation between jurisdictions, or alternatively their federal systems may have deficiencies that should be avoided (and therefore can provide examples about 'what not to do' within Australia's own federal system).

Most federal systems have had similar experiences in the division of powers in their constitutions. In general, the division of powers has been more fluid than possibly anticipated, and areas of concurrent responsibility have created disunity between powers:

While these realities have been present from the earliest days, they became qualitatively more significant in the twentieth century and in particular since the emergence of the active state from the 1930s onwards. The rising need for welfare and social policies spawned a new practice of shared programs and joint financing schemes. Social policy, which were generally the domain of the subnational governments, increasingly depended on fiscal transfers. Fiscal federalism ... became a main preoccupation of federal systems.¹⁵

Intergovernmental relations exist in all federal systems, regardless of the structure or history of the countries' institutions:

This flows from the inevitable fact of interdependence among their constituent governments, a result of the complexities of the contemporary policy agenda and the impossibility, even when the inspiration was to draw water-tight compartments, of drawing clear and separate lines of responsibility.¹⁶

In particular, older-style federations such as the United States, Canada and Australia, while attempting to provide for a division of powers in the constitution, didn't anticipate the fluidity and degree of overlap that would eventually be associated with such responsibilities. Those countries did not build formal intergovernmental arrangements into their constitutions. As a result, informal and ad hoc arrangements have developed for intergovernmental relations in those systems. In Australia, as '... in Canada, therefore, intergovernmental institutions must respect the overriding principle of accountability to executives of their respective legislatures. Rather than being part of the fundamental constitutional design, intergovernmental mechanisms are 'add-ons' responding to the reality of interdependence, but with little or no legal or constitutional status.'¹⁷

6 | INTERNATIONAL FEDERAL SYSTEMS: A BRIEF OVERVIEW

Hueglin and Fenna identify four basic models of federalism: Canadian; American; German; and European Union.¹⁸

Canada has an executive federal system with some powers allocated to particular levels of government and some concurrent powers in the constitution. Canada has a strong tradition of provincial autonomy. The lack of legitimate provincial senate representation as well as conflicts over the division of powers means that intergovernmental relations plays a politicised role, with policy making being competitive between the jurisdictions. Canada has an extensive system of intergovernmental relations. The provinces and federal government have ministers for intergovernmental relations. The intergovernmental relations are informal with the most predominant negotiations taking place at First Ministers' Conferences (FMCs) chaired by the Prime Minister and attended by provincial premiers. Regional Premiers' Conferences have also gained prominence on the intergovernmental landscape and more recently a Council of the Federation was established under agreement as an inter-provincial body. Two countries that have similar style federations to Canada are Australia and India.

The United States has a presidential federalist model. In the US, state governments have no direct access to the process of national law making and there is no formal institutionalised intergovernmental body or arrangement to deal with intergovernmental issues. This arises from the political system in the United States in which the federal and state governments are co-sovereign as well as the huge size and diversity of the political and social environment in the US. For example, there are 50 states and over 87,000 local governments in the US,¹⁹ and therefore there is great difficulty in developing a system that represents all of those interests and can reach a consensus view. Instead, most intergovernmental entities are ad hoc and short-lived committees, task forces and working groups created for intergovernmental lobbying and negotiation on specific issues. For example, states lobby the federal government through state organised institutions (e.g. National Governors' Association and National Conference of State Legislatures):

Intergovernmental relations also tend to take the form of 'picket-fence federalism' in which each policy field has its own intergovernmental relations. Federal and state bank regulators, for example, know each other and interact with each other ...

These arrangements have the advantage of dividing the huge intergovernmental system into more intimate, personal, and manageable set of relations. The disadvantage, however, is the difficulty of co-ordinating intergovernmental policy across fields.²⁰

Federal systems such as Mexico, Venezuela, Brazil and Argentina have adopted American-style federations with their own unique characteristics.



In Germany, the integrated federal model emphasises collective responsibility for legislation and implementation, and therefore more formalised and institutionalised intergovernmental relations. Most national legislation requires approval of the Länder governments in the Bundesrat before it is then implemented and delivered by Länder governments. Cooperation is also required for a number of constitutionally established joint tasks. There are regular prime ministerial conferences and summit conferences with the chancellor, aimed at coordinating legislative and policy cooperation. South Africa has adopted a variation on the German style of federation.

The European Union (EU) is a cultural federalist model consisting of member states with different histories, languages and social, legal and economic systems. Europe has two legislative chambers – a European Parliament representing European populations on a majoritarian basis and a Council of Ministers representing European governments. An executive European Commission is a government-appointed body of policy experts and acts like a cabinet. The principal intergovernmental decision making institution of the European Union is the Council of Ministers. The Council of Ministers makes decisions on proposals suggested by the Commission (the Commission proposes policies and legislation to the Council and is responsible for the administration and monitoring of implementation of treaties and decisions of the European Union).²¹

The European Union is based on the rule of law. This means that everything that it does is derived from treaties, which are agreed on voluntarily and democratically by all member states. Accordingly, the intergovernmental conferences of the European Union have enabled the successful agreement and establishment of several treaties for the European Union.

Spain has adopted an innovative intergovernmental relations mechanism in response to European integration. A 'Conference on Union Affairs' is held to establish Spain's position in European affairs (see Exhibit 4).

It is difficult to compare intergovernmental relations (IGR) in different countries. Such relations will be unique depending on many factors including the history and make-up of the country (e.g. nationalities, geography, and religious divisions), the type of federal system, the division of powers and the fiscal relationships:

Patterns of IGR, then are largely the result of such factors external to IGR itself. In none of these countries are institutions of IGR so strongly entrenched that they have strong independent effect on the behaviour of political actors. They are reactive and responsive, rather than determinative of the character of the federation. This is not to say, however, that policy makers in each of these countries can ignore the task of improving their machinery for co-operation.²²

It is also difficult applying the lessons from other countries to Australia, which has its own characteristics:

Because intergovernmental relations are for the most part the result of subconstitutional and often informal arrangements, it is not so easy to distinguish country specific models.²³

There are a number of challenges facing Australia that should be identified and tackled now, rather than in an ad hoc and reactive manner. This can only be achieved through better formal intergovernmental cooperative institutional mechanisms. The Victorian Federal–State Relations Committee in its report, *Federalism and the Role of the States: Comparisons and Recommendations*, commented that:

Although Australia's intergovernmental bodies have developed a great deal over the past ten years, they do not have the robust institutional character displayed by many of the institutions in the other federations visited by the Committee.²⁴

7 | PRINCIPLES OF INTERGOVERNMENTAL RELATIONS

What are the ideal principles that should guide intergovernmental relations?

1. EFFECTIVENESS

Intergovernmental relationships must be established so that they are capable of achieving policy objectives that have been set (and so that there is the capability of avoiding duplication and overlap).

2. TRANSPARENCY

Effective information about policy objectives and decision making must be in the public domain so that there is clarity around the bases for decisions and actions as well as greater pressure brought to bear on governments to maintain the federal reform agenda and be accountable for progress and outcomes of reform.

3. ACCOUNTABILITY

Governments must be subject to appropriate checks and balances to ensure their actions and decisions are scrutinised and justified.

4. EFFICIENCY

Intergovernmental relationships must be capable of achieving objectives in a timely manner free from political capture or stalling, and against a long-term vision.

5. INDEPENDENCE

Actions and decisions must be free from undue influence from political or private interests. They must have high-level commitment.

7.1 | EFFECTIVENESS

Intergovernmental relationships must be established so that they are capable of achieving the policy objectives that have been set (and so that there is the capability of avoiding duplication and overlap)

Recent experience in Australia suggests we need to be much better at anticipating barriers and opportunities. Bottlenecks in key export infrastructure and the lack of a strategic approach to tax reform are just two prominent examples of our failure to anticipate emerging economic challenges.

The record on cooperation and agreement across governments in Australia is not strong. At present, it can be too easy for one level of government to avoid its responsibilities by levelling blame at another. It can be too easy for governments to weaken their commitment to reform under pressure from vested interests. The pressure on governments to work cooperatively may only be intermittent.

Some key questions here are the extent to which intergovernmental processes ensure that there is:

- + An effective formal structure or mechanism to properly anticipate policy reform initiatives as well as ensure effective intergovernmental meetings.
- + Administrative mechanisms to facilitate appropriate analysis, research and national reform priorities free from parochial interests (including information and clarity of objectives as well as a commitment to using those structures on a regular and frequent basis).
- + Flexibility to determine innovative solutions.

AN EFFECTIVE FORMAL STRUCTURE OR MECHANISM

If intergovernmental relationships are informal, complex or uncertain, they can lead to inefficiencies. Instead, institutionalised and formalised frameworks can ensure that there is a clear framework for both policy research and identification as well as intergovernmental meetings. What should result from such institutionalisation is medium- and long-term development strategies – rather than ad hoc and reactive policy making.

The 2006 COAG agreements were positive, including the setting up of a new oversight body, the COAG Reform Council (CRC). Details of these initiatives, however, remain sketchy.

While the agreements at COAG appear to be a significant step forward, the process by which the agreements were reached actually highlights the weaknesses of the current institutional arrangements in our federal system of government.

It is debatable whether COAG members would have been willing to agree a new national reform agenda without considerable community and business pressure. Further, history has shown that COAG meetings can often be dominated by political positioning rather than policy leadership. Whether the ambitious reform work program and timetables agreed recently by COAG will be met will be a major test of intergovernmental cooperation and the institutional arrangements that underpin it. We therefore need to consider permanent institutional and structural arrangements to ensure the strengths of a federal system are captured, while its many pitfalls are avoided.

Should the intergovernmental arrangements be federal–state or interstate? Most federations have established arrangements of both forms. For example, Canada and Switzerland and more recently Australia, have recognised the need for interstate formal arrangements by establishing a forum for achieving consensus across state governments on issues, including federal–state issues.

On 21 July 2006, leaders of all Australian states and territories announced the formation of a new Council for the Australian Federation. The Council was inspired by Canada's Council of Federation (see Exhibit 3). South Australian Premier Mike Rann was appointed the inaugural chair of the council – the first of its kind since the Australian Federation was formed in 1901. It is proposed that the council will meet at least twice a year with members being the heads of each state and territory. There will be a permanent secretariat based in Canberra and funded by the states and territories. The chairmanship will rotate between Premiers and Chief Ministers on an annual basis. In brief, the functions of the council are to:

- + Find the best common position among states and territories of COAG-based agreements with the Commonwealth.
- + Where appropriate, reach joint agreements on cross-jurisdictional issues where a Commonwealth imprimatur is unnecessary, or has not been forthcoming.
- + Develop better procedures for the states and territories to share and exchange information and identify best practice policy and programs.
- + Anticipate future developments within the federal system, including decisions by the Commonwealth Government that might have a significant impact on states and territories.

The formation of the Council for the Australian Federation acknowledges the need to formalise and institutionalise such arrangements. However, the forum is an interstate arrangement. The exclusion of the national sphere of government can limit its effectiveness. In the Canadian context, this was discussed with respect to the inter-provincial Council of Federation, where it was thought that establishing a body to 'fight' against the national sphere might increase the tensions between the spheres rather than foster cooperation:

A true Council of the Federation would ideally include all the members of the federation. And despite the degree of decentralization that may have taken place in Canada during the past three decades, the federal government remains an important partner. To build a more powerful agency of the premiers at this time may simply serve to reinforce the cleavage between the two constitutionally recognized orders of government ... In contrast, a [national-provincial] Council of the Federation would begin with a bargaining position but hopefully end with tradeoffs and compromises necessary to produce a 'national' solution acceptable to most if not all parties.²⁵

What degree of institutionalisation (and therefore formality) is required? The types of forums that have been established across federations vary along a spectrum of formality (e.g. constitutional entrenchment) to informality (e.g. meetings called on an ad hoc basis).

The need for formal arrangements to ensure the effectiveness of intergovernmental relationships has been recognised in overseas jurisdictions. For example, a 1999 Intergovernmental Relations Audit conducted in South Africa described the intergovernmental relations framework in South Africa as 'a largely informal, interacting network at national, provincial and local levels, still relatively rudimentary but nonetheless developing into a method of intergovernmental relations, more or less appropriate to our institutional arrangements'²⁶ and recommended that due to the proliferation of informal intergovernmental structures, more coordination should be implemented in order to 'avoid duplication and ensure linkages with other IGR fora.'²⁷ In South Africa, there is use of statutory instruments to set up intergovernmental bodies. This led to the conclusion that: 'National government's powers of supervising and supporting provinces (and that of provinces in the case of local government) as well as the power of intervention by respectively national and provincial government should be spelled out clearly in legislation.'²⁸



The deficiencies associated with a lack of formal institutionalised arrangements can be seen in the Argentina's political landscape. With over 24 states and no formal institutionalised framework, many inefficiencies have resulted in the Argentinean federal system. While federal–provincial councils comprising of the federal minister responsible for the area in question and the provincial counterparts, have developed to deal with specific sectors such as education, domestic security, infrastructure, investment and public councils, they are associated with problems:

... these new opportunities serve more as forums for generating consensus than as bodies that make decisions that are binding on the parties. In many cases, valuable consensus developed after difficult deliberations are watered down over time because they are not implemented. Generally speaking, these organizations have lacked decision-making capacity and continuity over time, and have responded more to the political necessities of the day than to medium or long-term strategies. Finally, they are unable to replace negotiations based on personal relationships and the capacity to exert pressure with criteria may be unavoidably political in nature, yet at least established in advance of the particular negotiations under way and based on proper indicators.²⁹

Many believe that the Australian National Competition Policy (NCP) was an example of a successful outcome in a specific sector, providing a useful case study for what contributed to the success of the agreement. Factors identified as underpinning the success of NCP include:

- + Recognition by all governments of the need for reform.
- + Agreed priorities for reform.
- + A solid conceptual reform framework and program.
- + Strong procedural and institutional arrangements and mechanisms to address implementation issues and to monitor progress.
- + The provision of financial incentives for progressing agreed reforms.³⁰

What seems clear is that a degree of formality and institutionalisation is needed to make these arrangements work (especially for long-term implementation and monitoring). Various structures or mechanisms as examples are highlighted in the exhibits below. There are several different alternative arrangements that have evolved overseas in intergovernmental relations. For example, they may be constitutionally entrenched (and therefore more stable and formal) or evolve in an ad hoc manner as a response to specific economic circumstances:

The alternatives here range along a continuum. At one end intergovernmental deliberations are primarily about exchanging information and ideas, they provide a forum for discussion. In the middle are processes that emphasise bargaining, negotiation, and persuasion, but with the governments remaining responsible to their own legislatures and electorates for the actions they take. At the other extreme are intergovernmental institutions that can make formal decisions, binding on all the parties.³¹





Constitutional arrangement

A constitutionally entrenched institutional intergovernmental arrangement may have the benefit of certainty because no individual state will be able to remove its agreement or mandate. However, such an arrangement may lack flexibility. It may be possible to incorporate a degree of flexibility by granting the Commonwealth Government the power to legislate and vary the structure of the intergovernmental arrangements, if requested to do so by all the states.³² It would be very difficult to implement a constitutional amendment in Australia, however, given the difficulty associated with amending the Constitution by referendum. It is worth noting that the founding fathers of the Australian Federation recognised the need for an independent body to deal with trade issues arising from federation by incorporating a provision in the Australian Constitution for an Inter-State Commission: 'There shall be an Inter-State Commission, with such powers of adjudication and administration as the Parliament deems necessary for the execution and maintenance ... of the provisions of the Constitution relating to trade and commerce ...' (section 101 of the Australian Constitution). The Inter-State Commission was established by statute to fulfil this role, however it was allowed to lapse after the High Court found that its adjudicatory powers were in violation of the Constitution's requirement for a strict separation of judicial powers.

Statutory mechanism

A permanent formal intergovernmental body may be established by a scheme of uniform legislation. This approach would be advantageous because it would create a reasonably certain statutory arrangement which would be transparent and given the force of legislative power (such as other bodies created by legislation including the Australian Securities and Investments Commission and the Australian Competition and Consumer Commission). The degree of independence afforded a statutory body would be greater because of the certainty and entrenchment of the arrangements. The problem associated with this approach is that individual states may decide to remove their legislative mandate. However, such an arrangement would be more likely to be easily achieved than a constitutional amendment by referendum and might be able to be dealt with along the lines of the Inter-State Commission.

In some federal systems, the recognition of the need for intergovernmental relations has resulted in the development of a system of 'summitry'; for example, COAG in Australia, FMCs in Canada and the European Council in the European Union. In Australia and Canada, the lack of formality of those arrangements has had its problems. In the European Union, the European Council originated informally, and eventually it was agreed that it would meet twice yearly, in accordance with the council presidency, which rotates every six months among the member states, and that extraordinary meetings could occur on specific issues. The need to formalise such arrangements has been recognised. The yet-to-be-ratified constitutional treaty will establish the European Council as one of the EU institutions.³³





Government department

A permanent formal government department staffed by Ministers could be established. This approach would have the advantage of having certainty, transparency, funding and high-level support from government. It would, however, only operate at one level of government (e.g. Commonwealth) and while it may be able to assess federal issues it would have similar pitfalls to the Productivity Commission in that it is controlled by one level of government and takes its goals and objectives from government (rather than being able to independently determine its scope of work). The Department of Constitutional Affairs in the United Kingdom, for example, has some role in managing constitutional arrangements (e.g. courts, the justice system, human rights and modernising the constitution). However, as the UK is not a federation the arrangements are not directly applicable to Australia's federal system (see Exhibit 13).

Formal agreements

A formal agreement between levels of government may have the advantage of being more easily achieved. A formal agreement has been utilised by the Canadian provinces to establish the Council of Federation because a state may be able to remove its mandate (see Exhibit 3). Australia also saw the state and territory leaders announce the formation of the Council for Australian Federation. However, the arrangement may suffer from a degree of uncertainty and a lack of transparency. In Canada, the problems (such as short-termism) associated with an agreement were seen in a federal-provincial agreement in 1985, which contained a five-year commitment to annual conferences. However, it was not renewed despite strong provincial pressure to do so. The trend in recent years has been towards less frequent, and less formal 'First Ministers' Meetings' rather than 'Conferences'.³⁴

A series of conferences

The Intergovernmental Conferences in the European Union have worked well to assist in the development of treaties. However, they suffer from a lack of permanency and focus on a particular issue. A series of conferences is more likely to be a successful intergovernmental arrangement at a functional level, rather than a long-term economic policy perspective.

Another question is the level of institutionalisation of intergovernmental arrangements. What is clear is that the greater the formality, accountability and transparency that can be achieved at any level, the better the outcomes that can be achieved. The success of the NCP process shows that even at functional levels, a degree of formalisation can contribute to successful outcomes. Intergovernmental relations generally operate at two levels. On one level, political leaders will meet at some forum (e.g. conferences) and make reform decisions. Ongoing business then requires intergovernmental cooperation at a functional level. Although the functional processes of reform implementation are beyond the scope of this paper, it is worth noting that there are a number of innovative formal intergovernmental arrangements at a functional level.

In Australia, Ministerial Councils are convened regularly on various issues, with varying degrees of success:

The underlying logic in the Westminster system is one of adversarial, competitive, majoritarian, winner-takes-all politics. Despite frequent and eloquent calls for greater harmony and co-operation among constituent governments, this pattern tends to be reflected in the conduct of intergovernmental relations in Canada and Australia. This is especially so when issues rise to the senior political levels, and thus questions of overall strategy, power and status. In both countries – and in others such as the United States – co-operation is greater lower in the administration, where officials are more likely to share common professional values and similar clienteles.³⁵

However, because the meetings lack a public profile and those attending are not the Premiers and Prime Minister, there is a lack of accountability and transparency at a public level associated with the process. Although there may be some good outcomes associated with those meetings, there is no transparent method for the public to identify necessary reform areas or monitor the results of the meetings.

Similar functional arrangements exist in other jurisdictions to deal with specific sectors. They have an important role to play, but, like the Australian Ministerial Councils, they generally respond to reform issues that have already been identified and do not anticipate problems and are not accompanied by the required degree of high-level transparency and accountability.

In Canada, Ministerial Councils ‘... in recent years ... have greatly increased in number, have become more institutionalized, and have played a more formal role in carrying out mandates assigned by first ministers. These workhorses of the system now operate in fields such as social-policy renewal, forestry, transportation, education and the environment.’³⁶

In South Africa, a number of informal MINMECs (consisting of the relevant minister and provincial MECs) have been established. They deal mainly in coordinating concurrent national/provincial development. They coordinate policy development and the implementation of policies and legislation. The MINMECs are supported by Technical MINMECs, consisting of a senior official of the national department concerned and senior line functionaries from the provincial governments. The Technical MINMECs give technical and administrative support and advice to the political MINMECs. There is no provision for the enforceability of the decisions of these bodies.

In the European Union, there is a committee system that involves the informal interaction between member state governments and the European executive at a policy level. There is a committee for all of the EU’s main activities, and the members are policy specialists from the national government administrations. In Brazil, public consortiums have been established under federal law which aim to promote the common interest of various jurisdictions in certain matters.³⁷



State/private lobby groups

There is a strong history of state organisations and private organisations that lobby the federal government in the United States. While this may have achieved some successful individual outcomes, there are problems associated with inter-provincial bodies and lobbying tactics. They are ad hoc arrangements dealing with specific issues, rather than having a long-term objective and an economy-wide focus. Such a process enhances the conflict between the different levels of government and the purpose is to present a 'state' view rather than institutionalise agreement and cooperation between different levels of government. Accordingly, this form of institutionalisation would suffer from a lack of cooperation, accountability, long-term focus and independence.

Legally incorporated body

In Canada, those Ministerial meetings that have a set of formal institutional arrangements appear to have the greatest degree of intergovernmental collaboration. For example the Canadian Council of Ministers of the Environment is a legally incorporated body. It has a rotating chairmanship among the 14 jurisdictions on an annual basis and a permanent secretariat that is funded on a pro rata basis according to population. This has led one commentator to state: 'It is not surprising that the consistency and outcomes from this Ministerial grouping exceeds that of any other counterparts.'³⁸

Consideration should also be given to the institutionalisation of intergovernmental forums that may not be linked to government or political persuasions but instead carry a degree of independence. What has hampered collaboration and outcomes in many federations has been political 'jockeying' and buck-passing rather than long-term perspectives. There may be some alternative intergovernmental arrangements that achieve greater accountability, transparency and independence, and accordingly better outcomes (e.g. the Productivity Commission in Australia). (This is discussed in 'Independence' below).



While the full details of the powers and role of the CRC are yet to be worked out, the CRC is unlikely to be in a position to independently monitor the progress of COAG in implementing the national reform agenda or to initiate its own reviews of the economy and set new targets for future reform. However it is constructed, the CRC is unlikely to have a role in anticipating future economic challenges for consideration by COAG. Further, one of the challenges is to determine, where there is agreement, how it should be implemented and how progress on implementation should be monitored. Even where agreement is reached, there is potential for the implementation to be undone: 'Some unravelling of previous consensus is even evident in 'old' areas, like the national energy market.'³⁹

To ensure effectiveness of Australia's intergovernmental arrangements what is needed is the formal institutionalisation of a permanent independent intergovernmental body at a federal–state level as well as an independent body (to be called in this paper the Federal Commission). Such formalisation could be through a scheme of cross-jurisdictional uniform legislation, which has worked well in the United States (see Exhibit 8) or by formal agreement (but this may have less permanency and stability than a statutory arrangement.) Some examples of intergovernmental arrangements from other federal systems are highlighted below. They are not exhaustive, but illustrative of the different types of structures that have evolved.





FOUNDING AGREEMENT

EXHIBIT 3

CANADA – COUNCIL OF FEDERATION

On 5 December 2003, Canada’s Premiers set up the Council of the Federation under the Council of Federation Founding Agreement. It is an institution for collaborative intergovernmental relations. The Council of the Federation was created by Premiers so that the provinces and territories could play a leadership role in revitalising the Canadian federation and building a more constructive and cooperative federal system. The Council of the Federation’s objectives are to:

- + Promote interprovincial–territorial cooperation and closer ties between members of the Council, to ultimately strengthen Canada.
- + Foster meaningful relations between governments based on respect for the Constitution and recognition of the diversity within the federation.
- + Show leadership on issues important to all Canadians.

The governments of the 10 provinces and of the three territories of Canada, as represented by their premiers, are members of the Council.

The premiers of the provinces take turns chairing the Council according to the rotation established by the Annual Premiers’ Conference. The term of office of the chair is one year. The chair acts on behalf of the Council according to the mandates received from it.

The Council of Federation Founding Agreement provides that there will be an annual meeting of the Council of the Federation each summer in the province of the incoming chair. In addition, there will be at least one other meeting to be held in a province or territory each year in a location to be determined by the Council.

The decisions of the Council are reached by consensus. The Council may decide, from time to time, to hold special meetings to which it may invite the Federal Government.

A Steering Committee has been established, composed of the deputy ministers responsible for intergovernmental relations or such other representative designated by a member. The Steering Committee is chaired by the deputy minister of the province chairing the Council. The Steering Committee reports to the Council and assists the Council and supports the Committee of Ministers in the performance of their respective mandates. The Steering Committee prepares the meetings of the Council and carries out the study, research and analysis mandates that it receives from the Council, and sets up and supervises the Secretariat.

The Secretariat reports to the Steering Committee, which is also its board of directors. The head of the Secretariat is appointed by and reports to the board of directors. The Secretariat assists the Steering Committee in the preparation for meetings of the Council and performs any task that the Steering Committee assigns to it. The Secretariat is funded by the members on a pro rata basis, according to their respective populations.

The Premiers’ Council on Canadian Health Awareness is under the responsibility of the Council of the Federation, as is the Secretariat for Information and Co-operation on Fiscal Imbalance.

Some of the initiatives that have arisen from the Council include the national transportation strategy announced on 8 December 2005. The strategy recognises that the federation was built on a vision, expressed in a railway, to unite the country from coast to coast. Recognising that Canada’s provinces and territories have a range of differing infrastructure needs, premiers identified Canada’s transportation system as one of the most important foundations of the country’s international competitiveness and noted that it is key to ensuring a better standard of living for all Canadians.

Source: www.councilofthefederation.ca.



EXHIBIT 4

SPAIN – CONFERENCE ON EUROPEAN AFFAIRS

Spain's entry into the European Union triggered an innovative intergovernmental response. In a 1994 agreement, the national government and the Autonomous Communities set up a general Conference on European Affairs (as well as a number of policy-specific sectoral conferences) in order to coordinate Spain's position on European affairs. There are several meetings a year which are usually preceded by self-coordinating meetings among the Autonomous Communities (joint positions are decided on the basis of one vote per Community which are then communicated to the national government).

Source: TO Hueglin & A Fenna, *Comparative Federalism: A Systematic Inquiry*, Broadview Press, Canada, 2006, pp. 242–243.

EXHIBIT 5

RUSSIA – STATE COUNCIL

With 89 constituent units as part of the Russian federal system, there are clearly divergent cultural, economic, climatic and environmental factors between the units. There is often a lack of clarity in the division of powers in the Russian constitution, or a considerable degree of overlapping jurisdiction.

President Putin set up a consultative body in 2000 called the State Council. This body consists of all of the heads of the executive branches of the constituent units and meets quarterly at the request of the Russian President to discuss particular issues.

Within the State Council, a Presidium was set up, consisting of seven members drawn from the State Council on a rotating basis. Meeting monthly, the Presidium is able to discuss and analyse the major initiatives undertaken by the federal government.

Also within the State Council, various working groups prepare proposals for economic and political reform. The members of the working groups haven't been limited to State Council members and include 2–3 State Council representatives, highly qualified experts and other political representatives. Some of the areas that the working groups have been set up to deal with include federalism, energy production and distribution, improvement of federal administration and development of local government.

Source: JP Meekison (ed.), *Intergovernmental Relations in Federal Countries*, A Series of Essays on the Practice of Federal Governance, Forum of Federations, 2002, p. 67.



EXHIBIT 6

SOUTH AFRICA – PRESIDENT’S CO-ORDINATING COUNCIL

The President’s Co-ordinating Council is a non-statutory body and therefore its decisions are not formally binding or enforceable. It consists of the President (chairperson), the nine provincial premiers and the minister for provincial and local government. It meets twice a year. Its functions include the enhancement of the ability of provincial executives to make inputs on the formulation of national policies, the promotion of inter-provincial dialogue, dispute resolution at an inter-provincial level as well as between provinces and national government, improving cooperation between the national and provincial spheres of government (also as regards the strengthening of local government), and the coordination of cost-cutting programs (e.g. rural development and urban renewal).

Source: JP Meekison (ed.), *Intergovernmental Relations in Federal Countries, A Series of Essays on the Practice of Federal Governance*, Forum of Federations, 2002, p. 77.



STATUTORY INSTITUTIONALISATION

EXHIBIT 7

SOUTH AFRICA – VARIOUS INTERGOVERNMENTAL FORUMS

South Africa's federation is determined by the Constitution of the Republic of South Africa 108 of 1996. The Constitution recognises three tiers of government (federal, provincial and local). Further, there are 9 provinces in South Africa.

A number of intergovernmental forums have been set up under statutory arrangements to deal with specific issues.

For example, the Budget Council set up under the Intergovernmental Fiscal Relations Act 97 of 1997 consists of the Minister for Finance as chairperson and the MECs for Finance (Members of the Provincial Executive Councils) and the chairperson of the Financial and Fiscal Commission. The Budget Council must be consulted by federal, provincial or local governments regarding the provincial sphere, proposed policy or legislation affecting the provinces and issues relating to the management or monitoring of any provincial finances. No direct mechanism is made for an enforcement mechanism.

The Council of Education Ministers is established under the National Education Policy Act 27 of 1996. It consists of the Minister and Deputy Minister of Education and the nine MECs for Education (in their capacity as political heads of provincial education). Observer status is given to the national Director-General of Education and the chairpersons of the National Assembly's Portfolio Committee on Education and the NCOP's Select Committee on Education. Its functions include the promotion of national education policy, the sharing of information, the coordination of matters of national interest to the national and provincial government. In addition, the Minister must consult it before legislation is submitted to Parliament. No direct provision is made for an enforcement mechanism.

Amongst other statutory bodies are the Heads of Education Department Committee, Department of Foreign Affairs: Directorate Intergovernmental and Provincial Protocol, the Financial and Fiscal Commission and the Loan Co-ordinating Committee.

Source: JP Meekison (ed.), *Intergovernmental Relations in Federal Countries*, A Series of Essays on the Practice of Federal Governance, Forum of Federations, 2002, p. 77.

EXHIBIT 8

UNITED STATES – ADVISORY COMMISSION ON INTERGOVERNMENTAL RELATIONS

An American formal intergovernmental body was established from 1959–1996 called the Advisory Commission on Intergovernmental Relations (ACIR). ACIR was established by the 86th Congress (Public Law 86-380; 73 Stat 703) as a ‘permanent, bipartisan body of 26 members, to give continuing study to the relationship among local, state, and national levels of government’. The Act provided that the Commission would:

1. Bring together representatives of the federal, state, and local governments for consideration of common problems.
2. Provide a forum for discussing the administration and coordination of federal grant and other programs requiring intergovernmental cooperation.
3. Give critical attention to the conditions and controls involved in the administration of Federal grant programs.
4. Make available technical assistance to the executive and legislative branches of the Federal Government in the review of proposed legislation to determine its overall effect on the federal system.
5. Encourage discussion and study at an early stage of emerging public problems that are likely to require intergovernmental cooperation.
6. Recommend, within the framework of the Constitution, the most desirable allocation of governmental functions, responsibilities, and revenues among the several levels of government.
7. Recommend methods of coordinating and simplifying tax laws and administrative practices to achieve a more orderly and less competitive fiscal relationship between the levels of government and to reduce the burden of compliance for taxpayers.

The Advisory Commission on Intergovernmental Relations consisted of 26 individuals, three members of the President’s Cabinet, three U.S. House members, three U.S. senators, four governors, three state legislators, three country commissioners, four mayors and three private citizens.⁴⁰

Prior to the ACIR, there were other statutory intergovernmental bodies in the US such as the Intergovernmental Relations Commission. Many of the states in America have their own Advisory Commissions on Intergovernmental Relations that are also set up under statutes and are permanent intergovernmental bodies. For example, the Advisory Commission on Intergovernmental Relations (ACIR) for the State of Connecticut is a 24-member agency created in 1985 to study system issues between the state and local governments and to recommend solutions as appropriate. The membership is designed to represent the state legislative and executive branches, municipalities and other local interests, and the general public. The role of ACIR, as contained in Section 2-79a of the Connecticut General Statutes, is to: (1) serve as a forum for consultation between state and local officials; (2) conduct research on intergovernmental issues; (3) encourage and coordinate studies of intergovernmental issues by universities and others; and (4) initiate policy development and make recommendations to all levels of government. Six meetings of the ACIR are to be held in 2006. There are permanent staff and officers.

Source: <http://www.library.unt.edu/gpo/ACIR/Default.html> and <http://www.opm.state.ct.us/igp/acir/acircal.HTM>.

EXHIBIT 9

UNITED STATES – INTERGOVERNMENTAL POLICY ADVISORY COMMITTEE

One current intergovernmental consultative body in the US is the Intergovernmental Policy Advisory Committee (IGPAC) to the US Trade Representative (USTR). This committee was established in 1988 at the insistence of state and local officials who became concerned about the potential impacts of trade agreements, such as NAFTA and WTO, on traditional state and local powers. Each state needed to establish a ‘single point of contact’, usually in the Governor’s office.⁴¹

The IGPAC is a federal trade advisory committee composed of state and local officials appointed by USTR (or the President). IGPAC was formed with the Trade Act of 1974, and participation has varied over the years based on state and local officials’ concerns. IGPAC is comprised of representatives from the executive, legislative, and judicial branches of state, county and municipal governments, as well as associations of state and local officials.

The IGPAC, part of USTR’s statutory advisory committee system, is the committee charged with providing trade advice from the perspective of states and localities.

IGPAC is able to initiate its own work independently of USTR and also responds in reports to proposed trade agreements for the Administration and Congress. These reports are made public on USTR’s website.

Under the Uruguay Round and NAFTA implementing legislation, USTR also created the single State Point of Contact (SPOC) system, whereby the Governor’s office in each state designates a single contact to coordinate state trade policy input to the USTR. The SPOCs regularly receive Federal Register Notices, press releases, notifications and requests for advice on specific matters and are invited to participate in briefings and meetings.

Additionally, USTR officials frequently meet with gatherings of state and local representatives around the country at their annual meetings and conferences.

Source: www.ustr.gov.

AN INTERGOVERNMENTAL BODY – TO BE FORMALLY ESTABLISHED BY TREATY

EXHIBIT 10

EUROPEAN UNION – EUROPEAN COUNCIL

The European Union (EU) was set up to consist of the:

- + European Commission as the main policy-making executive.
- + European Council of Ministers as the main legislative body.
- + European Parliament as a secondary body of democratic representation and legitimacy.

However, like other federal systems, intergovernmental relations can evolve outside of the formal institutional arrangements. A need for intergovernmental meetings or ‘summitry’ was found to be required. What evolved were regular meetings of the European Council, which ‘soon became the most important agenda-setter for the EU even though they did not have a formal basis in the original treaties.’

The European Council, composed of the heads of government of the member states, meets twice a year to discuss the broader political and economic direction of the European Union. Each meeting is followed by a written report to the European Parliament and a verbal report by the President of the European Council.

The European Council originated informally, and eventually it was agreed that it would meet twice yearly, in accordance with the council presidency, which rotates every six months among the member states, and that extraordinary meetings could occur on specific issues. The need to formalise such arrangements has been recognised, and the yet-to-be-ratified constitutional treaty, will establish the European Council as one of the EU institutions.

Source: TO Hueglin & A Fenna, *Comparative Federalism: A Systematic Inquiry*, Broadview Press, Canada, 2006, pp. 239–240.

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SERIES OF MEETINGS FOR A SPECIFIC PURPOSE

EXHIBIT 11

EUROPEAN UNION – INTERGOVERNMENTAL CONFERENCES

The EU has an intensive network of intergovernmental committees and conferences involving senior levels of national civil services.

The Single European Act of 1987, which prepared the grounds for completion of the internal market, and the 1993 Maastricht Treaty, which established the EU in its current institutional form, were the result of European Council agreements. In both instances, the European Council initially established a so-called Intergovernmental Conference (IGC) for the preparation and drafting of the treaty revisions eventually adopted. The IGC are an ongoing series of intergovernmental meetings involving government leaders, ministers and the civil service. For example in the case of the IGC leading up to the conclusion of the Single European Act, the foreign ministers met several times between September 1985 and January 1986.

In addition to the IGC meetings, a European Council meeting in 1985 dealt with the single market and two 'working parties' of high-ranking officials negotiated the details in between the meetings.

Source: TO Hueglin & A Fenna, *Comparative Federalism: A Systematic Inquiry*, Broadview Press, Canada, 2006, pp. 239–240.

PRIVATE SECTOR BODIES

EXHIBIT 12

UNITED STATES – VARIOUS PRIVATE SECTOR BODIES

Because of the unique circumstances of the US political system, the private sector has an important role in intergovernmental relations.

About half of all federal aid to state and local governments is ultimately expended by private, non-profit organisations (i.e., NGOs) that perform public services, such as health and social welfare. Second, most high- and mid-level federal, state and local administrators are members of the same nationwide professional and scientific associations within their respective fields of policy responsibility and expertise. Within these associations, federal, state and local officials share information and interact with each other, while also interacting with relevant academics and colleagues in the private for-profit and non-profit sectors. These associations generate a considerable amount of intergovernmental co-operation and policy formulation by developing legislative ideas enacted by the Congress and/or state legislatures, adopting professional and scientific standards adhered to by all members, and performing intergovernmental dispute resolution functions.

Source: JP Meekison (ed.), *Intergovernmental Relations in Federal Countries*, A Series of Essays on the Practice of Federal Governance, Forum of Federations, 2002, pp. 4 and 35.

GOVERNMENT DEPARTMENT

EXHIBIT 13

UK – DEPARTMENT FOR CONSTITUTIONAL AFFAIRS

The Department for Constitutional Affairs (DCA) was established in 2002.

The Secretary of State and Lord Chancellor is supported by a Ministerial team, which, together with the Permanent Secretary and senior departmental officials, forms the Ministerial Executive Board. This Board benefits from the experience and input of non-executive directors.

The Ministerial Executive Board (MEB) is supported by a Departmental Management Board, chaired by the Permanent Secretary. The executive members of the MEB, together with the DCA Director of Human Resources, form the Departmental Management Board.

DCA is the government department responsible for upholding justice, rights and democracy: the foundations of a civilised society. DCA works from the simple rule that it exists to serve the public – not the providers.

The DCA's role is to drive forward the reform and improvement of the legal and justice system in England and Wales. It is responsible for upholding the rule of law and for reforming and safeguarding the constitution so that they serve the public effectively.

The DCA is also responsible for the administration of the courts in England and Wales (including HM Courts Service) and for the overall management of legal aid (through sponsorship of the Legal Services Commission). Also associated with DCA are a number of organisations such as the Public Guardianship Office, the Law Commission, the National Archives and HM Land Registry

Source: www.dca.gov.uk.

ADMINISTRATIVE MECHANISMS TO FACILITATE DECISION MAKING

A lack of administrative support, clear charter or objectives and processes can reduce the effectiveness of intergovernmental arrangements. For example, the Victorian Federal–State Relations Committee has commented in relation to COAG that:

... it is principally the Department of the Prime Minister and Cabinet that undertakes the preparatory work for the Council of Australian Governments' meetings. The Commonwealth thus dominates the operation of the Council of Australian Governments, inhibiting the capacity of the States to use it as an effective forum, and undermining its role as a federal decision-making body.⁴²

SECRETARIAT

In Canada, many federal–provincial meetings are provided with organisational and secretarial services through an intergovernmental body, the Canadian Intergovernmental Conference Secretariat. As federal–provincial relations have become more important, all governments have established offices, attached to the First Minister, to oversee the province’s intergovernmental affairs.⁴³ In addition to serving federal-provincial First Ministers’ meetings, the Secretariat serves the Annual Premiers’ Conference, the Eastern Canadian Premiers’ and New England Governors’ Conference and the Western Premiers’ Conference. The core of the Secretariat’s work, however, is providing services to multilateral meetings of Ministers and Deputy Ministers in virtually every sector of government activity. Although designated a federal department for the purposes of the *Financial Administration Act*, by an Order-in-Council on 29 November 1973, the organisation is in fact an agency of the federal and provincial governments. Not only is its budget supported by these two orders of government, but its staff is selected from both federal and provincial governments, and the Secretariat reports annually to all governments that it serves. The Victorian Federal–State Relations Committee commented that the permanent Secretariat serving different levels of government provides ‘an institutional ‘memory’ which eases executive decision making’.⁴⁴

Even in the United States where the focus is on lobbying by the states through organisations such as the National Governors’ Association and the National Conference of State Legislatures, those organisations have permanent secretariats to support the members of those organisations. The secretariats provide administrative, research and policy support and facilitate communication between members and the organisations.⁴⁵

INSTITUTIONAL SUPPORT

In Canada, the First Ministers’ Conferences have ‘no continuing institutional support,⁴⁶ no staff serving it, no routine procedure for following up business and reporting back. As a result, the frequency and usefulness of meetings has varied. The Annual Premiers Conferences (APCs) in Canada on the other hand, between the provincial premiers, have evolved into a more institutionalised body. APCs are held every August under a rotating chair and the meeting is supported by civil servants and an on-going agenda of work that connects one meeting to another. The assistance of civil servants enables the provision of position papers, issuing of communiqués and launching of projects to be undertaken by ministers.⁴⁷ Autonomous work can be initiated at the meetings. ‘It was at one of these meetings that the social-union initiative was begun, which resulted in the Social Union Framework Agreement (SUFSA)’.⁴⁸

The importance of institutionalisation through regularity of meetings and designated government staff can be seen in some of the commentary and analysis on the subject. One commentator writes in respect of the Canadian system:

When there is a commitment to the using the mechanisms on a regular basis, patterns of behaviour result. To take the most obvious and prominent example, the First Ministers Conference, holding regular such events helps to create an environment favourable to cooperation. First Ministers themselves have the knowledge that they will have full opportunity to discuss their concerns with their colleagues. Not unimportantly, they come to know each other better. Of equal or possibly greater significance, their staff have to engage with each other in the preparation of such major events and in looking after the follow-up. This dynamic helps to establish a network of individuals accustomed to working with each other, developing a level of familiarity, confidence and trust that enables them to engage in collaborative ways to help minimise conflict.⁴⁹

In 2003, in response to the ad hoc nature of the other federal–provincial institutions in Canada, the Council of Federation was set up between the provincial premiers and territorial leaders. Set up under a Founding Agreement it also establishes a permanent steering committee and a permanent Secretariat. Federal and provincial governments staff the steering committee, which reports to the Council, and provides research (among other things). The body is funded by the members on a pro rata basis and meets at least twice yearly. The Council does not include the Prime Minister, but ‘such inclusion may only be a matter of time’.⁵⁰ If successful, the Council would signal a profound transformation of the Canadian federal system, from a classical parliamentary federation to a new model more akin to the German and European council governance.

In Germany, the Conference of Minister-Presidents has a preparatory stage whereby the heads of state chancelleries and senate chancelleries and the head of the Federal Chancellery meet one week prior to the conference. For the conferences of specialised ministers, the state secretaries of all the ministries at the Länder and federal level meet one week before the conference.

It appears therefore, that in order for the intergovernmental relations to be successful, a degree of formal institutionalisation is required, including regular meetings, sufficient resources and support from civil servants, an independent and rotating chair, an agenda that connects one meeting to another, a contributory funding formula, the ability to initiate projects autonomously and a framework for following up business and reporting back. These are essential elements of a system that operates well and facilitates successful outcomes.

In Canada, one commentator notes that there are lessons that can be learned from the different types of intergovernmental mechanisms that have developed in that country:

The lesson I draw from the forgoing is that if you are serious about getting significant results from intergovernmental relationships, the likelihood of success is greatly enhanced if there is a pattern of regular meetings (not at the whim of the chair), a secretariat to ensure that the necessary work is done, and a contributory funding formula. On the point of the secretariat, experience shows that if you want to have truly integrated efforts, you need the assistance of a dedicated staff, whose sole function is to prepare the Conference to do the work desired and to ensure there is follow up action to the meetings. The additional benefit of the presence of a secretariat is that it provides a responsibility point separate from the chair, and can provide the continuity needed in view of frequent changes of government and political leadership. In cases where sustained effort is required, a professional dedicated secretariat can be the ‘keepers of the flame’.⁵¹



In Canada, it was noted that significant investment in the machinery of the processes was important to achieve tangible outcomes. A secretariat is an important element of that machinery because it provides a permanent watch on the federalism agenda and facilitates continued cooperation between governments:

The dividing point between the transitory and the more substantial processes seems to occur around whether there is sufficient commitment to working collaboratively to establish a permanent secretariat. That is the point at which individual governments or agencies begin to give over some functions to a shared effort, and it generally entails a financial contribution. Comparison with international examples, notably the European Community, would seem to support this finding.

Establishing a secretariat means creating a staff that has as its sole purpose the advancement of the common goals of the parties. Other advantages are that having an ongoing centre of coordination allows an intergovernmental effort to weather electoral cycles, changes in leadership, and varying levels of commitment, all the while maintaining a consistent purpose and identity.⁵²

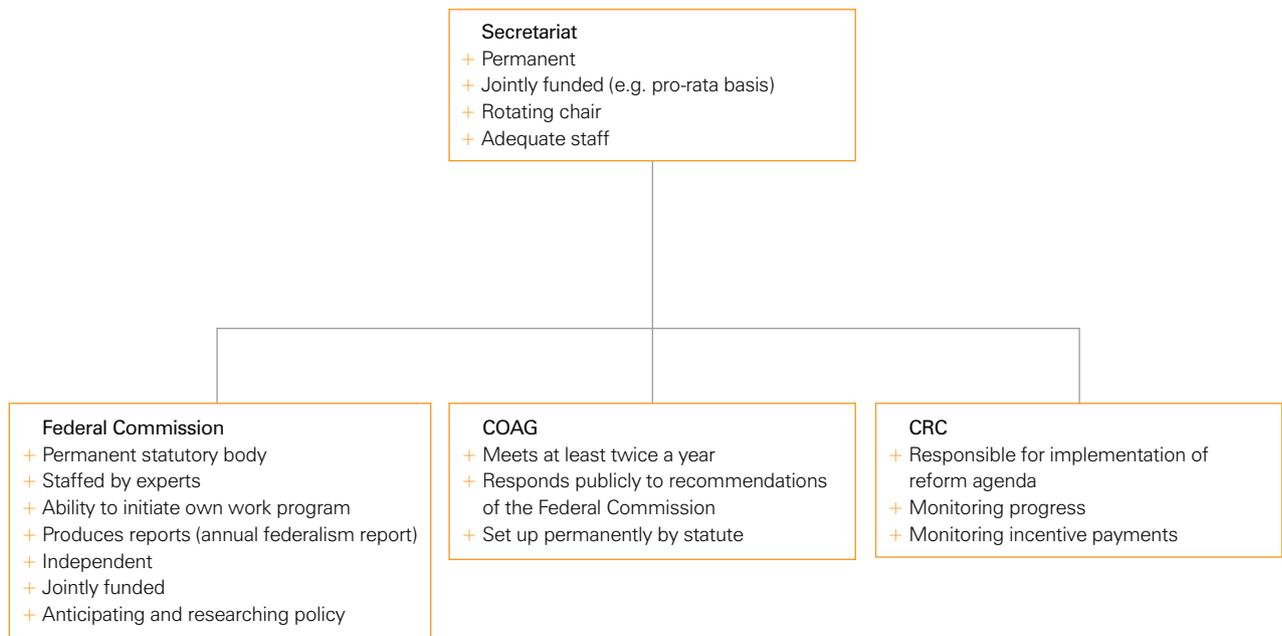
The Victorian Federal–State Relations Committee recognised the benefits to be gained from permanent administrative arrangements to support COAG, stating:

An Intergovernmental Secretariat would not only enable an increased workload to be met; it would also reduce the political control exerted by the Commonwealth over the Australian intergovernmental process, and would enhance the institutional character of the Council of Australia Governments by creating a sense of continuity between meetings.⁵³

Conclusion: To ensure effectiveness, adequate administrative arrangements may be required including the establishment of a permanent intergovernmental Secretariat to provide administrative and policy support (to the CRC, the Federal Commission and COAG); an independent and rotating chair; and sufficient resources (e.g. staff). Other considerations are whether there should be consensus or majority voting mechanisms, the funding of both the Secretariat and the Federal Commission and the role of the Secretariat (e.g. research and agenda setting).



FIGURE 1 A POTENTIAL STRUCTURE FOR THE FEDERAL SYSTEM



FLEXIBILITY TO DETERMINE INNOVATIVE SOLUTIONS

The relationships need to be flexible enough to accommodate changing policy perspectives and ideals in society. Therefore the options available for solving problems and the division of powers should not be rigid, but those options should be capable of meeting the challenges of a changing economy. Accordingly what is required is officials at a high level who have the power to make decisions and regular meetings and relationships that can ensure there is the flexibility to determine innovative solutions.

Other considerations associated with effectiveness are the frameworks and options for enabling agreement on various issues. In Australia there have been many examples of the flexible and workable solutions that have arisen from intergovernmental agreement making (e.g. mutual recognition, harmonisation).

While the possible options for agreement making and the division of responsibilities are beyond the scope of this comparison paper, what is clear is that there have been numerous and flexible agreements on a variety of issues. Intergovernmental negotiation must therefore have the capacity to recognise the flexible arrangements that are available, and not to be constrained by historical or other perceived constraints. For example, in Canada the 1995 Agreement on International Trade and the 1999 Social Union Framework Agreements included sections on dispute resolution and avoidance.⁵⁴ Similar mechanisms for ongoing implementation review and negotiation could also be incorporated in Australian solutions to ensure the effectiveness of any outcomes reached.



In Canada, the Council of Ministers of the Environment (discussed previously), in the absence of clear constitutional assignment of authority, were able to assign roles and responsibilities to particular governments based on two key principles: a single-window approach and the assumption that roles should be assigned to the government best able to carry them out.⁵⁵ Accordingly, experts that are capable of determining frameworks and innovative solutions will be necessary.

Cooperation and agreement is needed in key areas of the Australian economy to ensure that innovative solutions can continue to be found in the future. For example, one commentator has argued in relation to health:

While it was necessary to have a consistent national framework, the way in which health care is organised and delivered should vary across States to suit local circumstances and local community priorities. Indeed, a strength of federal systems is the diversity they allow which is most conducive to policy innovation and service improvement ... a complete redesign of the current system involving the integration of Australian and State Government health care programs through funds-pooling and budget holding – implemented to suit each State’s circumstances – was necessary if the underlying problems were to effectively addressed ...

In practice such a redesign would be “complex, difficult and time-consuming”. It would also require a great deal of collaboration among the Australian and State Governments in respect to governance systems, organisational and workforce development, as well as considerable institutional effort to support change.⁵⁶

Previously discussed were the reasons that NCP was successful. These included institutionalised monitoring mechanisms to ensure implementation of agreements and monitoring incentive payments. Accordingly, the CRC will need to be set up – with appropriate institutionalisation – to ensure its monitoring processes are adequate.

Conclusion: To ensure effectiveness, institutional governmental arrangements also need to have a sound ‘theoretical’ framework and basis for decision making, including the flexibility to determine innovative solutions. For example, mandated principles of federalism/goal setting as a framework for dividing responsibilities may be one method as a basis for decision making.

7.2 | TRANSPARENCY

Effective information about policy objectives and decision making must be in the public domain so that there is clarity around the bases for decisions and actions as well as greater pressure brought to bear on governments to maintain the federal reform agenda and be accountable for progress and outcomes of reform.

Transparency is needed to ensure the actions and decisions of the political decision makers can be judged against the policy objectives being pursued, and greater credibility is given to the findings of those who have met and negotiated outcomes.

High levels of transparency also increase the understanding of and commitment in the community to the recommendations of the political leaders and the reasoning behind the recommendations. One study of the intergovernmental processes in Canada has identified transparency and accountability as a significant factor in the success of intergovernmental relationships, stating:

The failures ... lies not in the lack of ability of our players and processes to find solutions, but rather in the inability to gain the public understanding and acceptance deemed necessary to ratify the products of negotiations ... A more detailed critique of executive federalism was ... that the practice was unduly secret, fostered a low level of citizen participation, weakened accountability to legislatures and frustrated matters making in onto the public agenda, leading to unresolved conflicts between governments.⁵⁷

Accordingly, transparency can be increased by publicly available agendas for intergovernmental meetings as well as publicly available reports outlining outcomes or recommendations from meetings. The influence such agendas and reports will have on governments should be increased by the public availability of the documents, therefore ensuring that there is sufficient pressure on governments to consider and implement agreed reforms.

One commentator has asked:

How open, transparent, responsive and accessible are the mechanisms established for the conduct of the IGR? The more important these processes are in the political life of a society the more it is necessary to subject them to the same democratic tests as are applied to other institutions. The question of the possible 'democratic deficit' is common to all systems of multi level government – indeed it was invented to address problems in the European Union.⁵⁸

Successful intergovernmental relations that have resulted in concluded agreements, have a number of characteristics that can act as a guide towards formulating a useful model for Australian intergovernmental relations. For example, the conclusion of intergovernmental agreements in Canada such as the Constitution Act 1982 and the 1980 National Energy Program (NEP) have had a number of similar characteristics including:⁵⁹

- + Open lines of communication.
- + Officials doing preparatory work identifying all the issues that need to be addressed, terminology used, data required, assumptions made and points of contention.
- + Dampening expectations as to probable outcomes and refraining from dire predictions.
- + Determining where compromise lies and looking for new innovative solutions.

For example, open communication lines and transparent information means that different viewpoints can be identified and assessed prior to the meeting. This enables background research and ideas to be developed. 'Clearing out the underbrush' in this manner proved useful in the Canadian NEP negotiations when 'both sides working together conducted a detailed analysis of the different assumptions and consequences on which the two positions were based.'⁶⁰

In the United States, there has been discussion about the Intergovernmental Policy Advisory Committee (IGPAC) to the US Trade Representative (USTR). For example, a non-profit public interest organisation called Public Citizen writes that:

Inherent structural problems make the IGPAC inadequate to the task of ensuring that state and local governments are provided a meaningful opportunity to give their prior informed consent before being bound to trade agreement rules. IGPAC members are selected by, and serve at the will of, the USTR. Even so, USTR is not required to respond to the committee's recommendations. IGPAC's comments to USTR are general, rather than covering state-specific commitments to trade agreement obligations. Only 22 states are currently 'represented' on the 48-person committee. Plus, representatives from a state are not representing that state in an official capacity, but rather are appointed to represent general state and local interests.⁶¹

Conclusion: To increase transparency there are a number of methods that can be employed. For example, if a Federal Commission were established it could provide independent and publicly available reports to COAG on policy items. Such reports could make recommendations, which would encourage all governments to consider the issues. Further, if a Secretariat were established then publicly available agendas and preparatory material could be developed prior to any meeting of COAG (agendas must flow from one meeting to another) – this would enable public discussion of policy items prior to the meetings.

7.3 | ACCOUNTABILITY

Governments must be subject to appropriate checks and balances to ensure their actions and decisions are scrutinised and justified.

The outcomes and recommendations of intergovernmental meetings and negotiations must have sufficient credibility in order to ensure that governments are motivated to properly implement the recommendations. A method of achieving greater credibility and accountability is through sufficient quality research to back up the recommendations. High levels of transparency increase accountability. In addition, good governance structures are necessary to ensure that the political leaders are accountable for the outcomes.

Accountability is necessary on a number of levels. Firstly, accountability forces governments to actually identify and assess reform issues and therefore to hold regular and necessary meetings between jurisdictions. Without such accountability, the governments may more easily be able to avoid having to deal with issues at all.

Secondly, accountability of responsibility for reform issues that are identified is necessary to prevent different layers of government from 'buck-passing' and for actual implementation to take place. If there is 'buck-passing', necessary projects and reforms may not be implemented, because there is no-one responsible for them. This may be enhanced by a transparent intergovernmental relations process, with clearly identified outcomes and publicly allocated responsibilities. Some degree of accountability can be achieved by appropriate fiscal arrangements (discussed in more detail below). However, institutionalised arrangements should also be directed at ensuring accountability can be achieved. For example, each of the meetings must be linked together (e.g. via appropriately drafted agendas and pre-prepared research papers) to ensure that continued accountability for reform is maintained.

Currently, the process in Australia has become captured by political interests, at the expense of the economy and certainty. Even where there has been an agreed distribution of powers, political interests can impact on the processes. This has been seen recently with the Corporations Act. While the states were due to refer their powers for a further period of time to the Commonwealth, the process was caught up in political jockeying, which had a negative impact on certainty and the operations of business. These sorts of events should be limited through accountability mechanisms, to ensure the avoidance of harmful actions that negatively impact the economy.

EXHIBIT 14

CORPORATIONS ACT AND REFERRAL OF POWERS

‘State governments are leaving it to the last minute to renew crucial legislative measures underpinning the national system of corporate regulation, creating uncertainty for business, investors and regulators.

The states have been angry that the federal government used its own constitutional power over corporations to support its new Work Choices legislation, which overrides state industrial legislation.

There has been concern in Canberra that the big Labor states are retaliating by failing to make the referrals needed to underpin the Corporations Act until the last minute. The Corporations Act effectively relies on a mixture of state and federal constitutional powers because of High Court rulings in the 1990s curtailing the federal government’s own powers.’

Source: M Davis, ‘States Let Costello Sweat on Business Law’, *The Australian Financial Review*, 2 June 2006.

In Germany, the problems with a lack of accountability have been seen:

Since 1969 the trend towards the unitary federal state has been considerably increased by the fact that, in practice, a comprehensive integrated system was installed through the introduction of tasks in which the federal government partly finances original tasks of the Länder (e.g. the building and extension of institutions of higher education, the improvement of the regional economic structure, the improvement of the agricultural structure and coastal protection, research funding) and through the creation of common taxes (income and corporate tax (turnover tax)). Based on the American models, this integrated system was called cooperative federalism. In the meantime this system has not only proved to be crippling, but also problematic from the democratic point of view, because everybody can be made responsible for everything, and therefore nobody is responsible for anything. For this reason efforts are currently being made to break up this integrated system again, thus achieving greater transparency with regard to decision-making and responsibility, and permitting more competition between the federal government and the Länder. However, despite these efforts Germany is still far removed from having a system of pure competitive federalism.⁶²

In Canada, a lack of transparency has been shown to potentially reduce the success and the accountability of outcomes. The First Ministers Conferences (FMCs) for example can vary in their transparency and therefore the accountability of the meetings to the public and their understanding of the processes:

The failures, and that is the judgement that almost universally attaches to these exercises, lies not in the lack of ability of our players and processes to find solutions, but rather in the inability to gain the public understanding and acceptance deemed necessary to ratify the products of the negotiations.⁶³

.....

Commentators have suggested that one of the best examples of significant reform in Australia was the National Competition Policy (NCP) and that its success was due to, among other things, a strong level of leadership and that:

If we could replicate it, I think it would be a step forward. It is not a bad model because it had an accountability aspect to it.⁶⁴

Every so often in Australia, certain strong personalities of leaders will result in some useful outcomes at COAG and productive reform agendas being established. However, it is inadequate that such a process depends entirely on the personalities and attitudes of leaders. Instead mechanisms should be established to ensure that federal issues and agendas are a consistent issue of politicians and not driven by particular personality types.

Accordingly, there needs to be a level of leadership and independence to ensure that reform initiatives are consistently assessed. Heads of government should view intergovernmental cooperation as an ongoing obligation, rather than an ad hoc reactive process. The Victorian Parliament's Federal-State Relations Committee commented:

In Canada, a majority of governments have a Minister for Intergovernmental Relations, who is able to assist the Premier or Prime Minister in dealing with these matters. Adopting this in Australia would increase the political and bureaucratic focus on intergovernmental matters, and would allow an appropriate political authority to manage and direct the business of intergovernmental relations. A Minister with responsibility for intergovernmental relations would ensure continuity in each States' approach to intergovernmental relations. The Minister may be directly involved in all intergovernmental negotiations, or support other Ministers involved in such negotiations.⁶⁵

Conclusion: Accountability can be increased by ensuring that an independent body to do research on policy issues is established – called a Federal Commission in this paper (see discussion in 'Independence'). The Federal Commission should have a clearly publicised charter (e.g. its make-up and objectives and role). The outputs of the Federal Commission should also be made public. Further, accountability can be increased by more frequent meetings of COAG (see 'Efficiency') as well as a Secretariat (see 'Effectiveness'), which will ensure that there is a continued dialogue and agenda that the participants must address and cannot avoid.

The preparation of agendas for COAG meetings should link the meetings together – creating an ongoing accountability of ideas. The transparency of discussions, agreements and outcomes of COAG – with clearly allocated lines of responsibility – may also increase accountability.

For governments, a Minister for each level of government should be given the responsibility for intergovernmental relations.

7.4 | EFFICIENCY

Intergovernmental relationships must be capable of achieving the objectives in a timely manner, free from political capture or stalling, and against a long-term vision.

While political pressure can build up to overcome short-term political and parochial interests, commitments to reform are meaningless unless they are implemented fully and in a timely way. Elections, leadership changes and reaction from vested interests, including in business, can undermine the reform agenda and erode political will over time.

While there is currently some appetite for a national reform agenda across governments in Australia, this has not always been the case. Accordingly, the intergovernmental arrangements must ensure that there is continuing commitment to a national reform agenda over the long term, and to ensure that any agreed reforms are properly implemented despite potential changes in political will.

Currently COAG is the main forum for policy setting, but the problems with this forum can be short-termism and political capture. Accordingly there needs to be a force that can raise issues of importance to the economy that may not be politically palatable. A Federal Commission could be a permanent standing body that is able to conduct its operations free from political dynamics and in an efficient manner despite a changing environment. In addition, the funding and independence of the intergovernmental body must be assured to enhance the effectiveness of the intergovernmental operations in a changing political and social landscape.

There is a need to constantly assess the state of the economy and ensure it is operating in an efficient, effective and competitive manner. While the meeting of COAG in June 2005 appeared to be successful, John Howard commented afterwards that it was the most cooperative and productive of its kind that he had attended in nine years as Prime Minister. It is inappropriate for the key intergovernmental body to have only had one productive meeting in nine years and for such relations to only take place in times of limited opportunity.

EXHIBIT 15

WINDOWS OF OPPORTUNITY ARE NOT ENOUGH

... there was currently a rare opportunity for progressing economic reform at a national level, both in relation to completing unfinished business under NCP and to embracing new initiatives discussed at the June 2005 meeting of CoAG. One participant spoke about 'six months of blue sky' between electoral cycles 'a window of opportunity that we want to make the most of if we can.'

Source: Productivity Commission, *Productive Reform in a Federal System*, Roundtable Proceedings, Canberra, 2006, p. 14.



It was outlined previously that governments have three roles to play: anticipation, agreement and implementation. All three of these aspects must be capable of being delivered in an efficient and timely manner. Further:

The value of ongoing and frequent intergovernmental meetings should not be discounted. In the final analysis, effective intergovernmental relations are dependent on strong personal relationships and mutual trust and respect between individuals.⁶⁶

Regularly scheduled meetings have been found to be useful in some overseas intergovernmental models. In Canada, for example, the meetings of Ministers of Finance and their deputies have been found to be successful because of their regularity since 1941 and the build up of 'trust ties' among those involved in the process. While the meetings are not conflict free, the regularity of the meetings has ensured that the people involved in the meetings know and trust each other. This increases the likelihood of understanding each other's perspectives and hence finding mutually agreeable and workable solutions. The benefits of such regular meetings have been described as follows:

They have ongoing opportunities to exchange views and search for workable solutions. A great deal of information is exchanged and those involved in the processes experience and face common problems, whether they be inflation, tax policy or deficit reduction. The personal relationships that develop have been an important factor in overcoming many of the irritants which arise and which have the potential of escalating into more serious problems.⁶⁷

In Canada, the First Ministers Conferences are a gathering of provincial premiers and the Prime Minister of Canada. The meetings are called by the Prime Minister and their frequency has varied according to the preference of the Prime Minister of the day:

From 1927 to 1944, there were approximately eight federal-provincial conferences involving First Ministers, ten from 1945 to 1959 and fifteen from 1960 to 1969. After the constitutional conferences of 1969-1971, federal-provincial conferences at the level of Ministers and First Ministers became incorporated as an integral and regular component of governance in the Canadian Confederation. Federal-provincial conferences may involve meetings of the First Ministers (Prime Ministers), meetings of Ministers or meetings of Deputy Ministers and officers of agencies representing different levels of government and sponsored by their ministers.⁶⁸

Regularity also ensures that there is a permanent agenda that governments must be addressing, and therefore increases governments' accountability to that agenda.

Meeting regularly creates the assurance that there is a 'table' to which to bring initiatives or irritants. Equally important, it provides for a level of familiarity between the First Ministers and an opportunity for the public to become knowledgeable about the process, issues and viewpoints.⁶⁹



In Germany, the Conference of Minister-Presidents meets at least twice a year, while the conferences of specialised ministers meet at least every six months. The provincial governments or Länder in Germany have a unique position because they have an ability to influence federal legislation through the Bundesrat. The Länder are entitled to introduce bills into the Bundesrat and have a power of absolute or suspensive veto in certain matters. A process of political consultation and coordination between the Federal Chancellery and the Bundesrat has been developed whereby:

A Minister of State on the level of Parliamentary State Secretary has been entrusted with this task ... His main point of contact at the Bundesrat is its consultative Council, which is composed of 16 Land plenipotentiaries representing Land interests vis-à-vis the Federation. As a rule, this body meets with the Minister of State at the federal Chancellery on a weekly basis. They primarily come together to prepare Bundesrat meetings. They also discuss on a confidential basis, all other issues requiring co-ordination between the Federation and the Länder.⁷⁰

The Victorian Constitutional Committee has recognised the comparative deficiency in the number of intergovernmental meetings that have been held in Australia compared to overseas jurisdictions. Since 1990 there have been four Special Premiers Conferences, one Heads of Government meeting and seven Council of Australian Governments meetings.

In Germany and the European Union, intergovernmental bodies meet far more frequently than they traditionally have in Australia. The European Council meets every six months, and the Council of Ministers meets, on average, nearly twice a week. German Heads of Government meet every two to three months, and the Bundesrat sits in plenary session every third week. The Bundesrat must also be convened if demanded by the Bund, or at least two Länder.⁷¹

Conclusion: To ensure efficiency there must be an agreed number of meetings of COAG per year (e.g. at least 2 per annum) as well as agreement that COAG will respond to the recommendations of the Federal Commission in a given time frame.

7.5 | INDEPENDENCE

The actions and decisions of intergovernmental relations must be free from undue influence from political or private interests. They must have high-level commitment.

The Productivity Commission has a very important role in Australia's economic competitiveness in identifying reform priorities for Australia, and conducting detailed research and making recommendations on potential solutions. The Productivity Commission's contribution to the understanding of our federal system has been seen in a number of reports it has produced, including the recent compilation of materials from the 2006 Roundtable Proceedings in Canberra entitled *Productive Reform in a Federal System*. The Productivity Commission's role in federal–state relations is limited however:

- + The research priorities are set by the Commonwealth Government (and therefore potentially guided by political interests of the day rather than long-term objectives) and there is limited opportunity for the Productivity Commission to set its own work priorities.
- + There is no 'buy-in' by the state governments (either in terms of the direction of the Productivity Commission's work agenda, the funding of the Commission or the outcomes).
- + There is no requirement for the Commonwealth Government to respond to the reports of the Productivity Commission, and therefore less accountability for the findings.

Two considerations relating to independence are:

1. Ensuring that a research body such as the Federal Commission is able to consider reform priorities and initiatives that may not be politically palatable as well as propose solutions without influence from political interests (e.g. division of powers between levels of government).
2. In addition, COAG requires some independent, institutionalised mechanisms to ensure that it is not captured by one specific jurisdiction/level of government.

SETTING ITS OWN WORK PRIORITIES

The Federal Commission should be free to achieve the policy objectives without interference (including political, financial and operational independence). As a matter of principle, the greater the independence, the greater should be its level of accountability and transparency. Just some of the reasons that independence is important are the need to establish a credible and expert body; ensure a degree of transparency and accountability to the wider community; and create a long-term stable economic environment free from short-term political or private sector influences.

Independence may be achieved by ensuring that the body is staffed by representatives and experts from a variety of backgrounds and political influences, including from both state and federal government. Some examples of where there are experts/private individuals involved in intergovernmental relations are the working groups within the Russian State Council and the US Advisory Commission on Intergovernmental Relations (see Exhibit 5) and the Health Council of Canada (see below). Similarly, the intergovernmental body should be jointly funded by state and federal government so that it is not reliant upon any one sphere of government. This was seen in the funding arrangements in the Canadian Council of Federation.

The Council of Australian Governments is currently an ad hoc body. Meetings are called by the Prime Minister, and much preparatory work is undertaken by the Department of Prime Minister and Cabinet. This means that the Commonwealth dominates the Council. Mandated meetings of the Council of Australian Governments would enhance the Council as a forum for joint Commonwealth–State decision making.⁷²

INSTITUTIONAL MECHANISMS

The Federal Commission must therefore be able to form its own work program and create its own agenda, so that it can review aspects of the economy that may not be politically expedient or agreeable. This should allow the problems associated with buck passing or lack of agreement across governments to be avoided.

In order to be effective, the Federal Commission must also be sufficiently funded so that it can conduct wide ranging reviews and be staffed by experts. The staff must have sufficient knowledge and experience to be able to make economy wide assessments about the future of Australia's economy and to make recommendations about a national reform agenda.

It was encouraging that the most recent COAG communiqué in July 2006 outlined more details about the COAG Reform Council (CRC), which was proposed to be independent and would comprise up to six members. The CRC will comprise a Chairman appointed by the Commonwealth, a Deputy Chairman appointed by the states and territories, and four members to be agreed by COAG, with at least one member having the appropriate skill sets with regional and remote experience. COAG would agree on staffing arrangements for the CRC. However, it still remains unclear what the exact role of the CRC would be but it will be primarily involved in monitoring implementation and therefore unlikely to be anticipating or researching new policy areas. In particular, it is unlikely to have the opportunity to initiate its own work and to anticipate new challenges facing the economy.

As previously discussed, many mechanisms for intergovernmental relations, where they are not formalised and institutionalised, will vary in their frequency and transparency depending on the political will of the leaders at the time. It is essential that the frequency, transparency and accountability are not determined by the political agendas, but that there are mechanisms for forced regularity of meetings, monitoring the progress of agreements and implementation of reform on an on-going basis.

In Canada, the politicisation of the intergovernmental process led to a loss of legitimacy of the process and a lack of satisfactory outcomes:

A new type of 'summit federalism' began to emerge, with all the paraphernalia of international conferences, flags, government limousines, rolling cameras, and press conferences after lengthy and often night-long meetings behind closed doors. Yet all the orchestrated hype could not prevent the eventual constitutional settlement of 1982 being concluded without Québec. After Trudeau's departure in 1984, two further attempts of bringing Québec into the constitutional fold ultimately failed because the process itself had begun to lose legitimacy and because support for the recognition of Québec as a distinct society faltered in English Canada.⁷³

High-level leadership is crucial to ensure that reform priorities are consistently monitored. Without institutionalised mechanisms to pressure those high-level leaders to meet and agree a reform program, reforms will stagnate. For example, the NCP reforms in Australia were an example of successful outcomes from intergovernmental relations. However, commentators have highlighted that the 'difficulty of replicating it, of course, is that the circumstances that gave rise to the NCP are almost totally unlikely to emerge again.'⁷⁴



Further, it is essential that the intergovernmental arrangements have independence to ensure the regularity of meetings as well as adequate outcomes from the meetings. The lack of such independence of COAG has resulted in various problems, including infrequent meetings, lack of transparent agenda and decision making and politicised outcomes. Indeed 'COAG meets only briefly and only once a year ... The underlying reality, though, is not entirely consistent with this image. COAG has no statutory – let alone constitutional – foundation; it has not changed the powerful imbalance in Australian federalism; and it is an institution existing and functioning at the pleasure of the Prime Minister.'⁷⁵

Finally however, it must be recognised that our democracy depends on the elected representatives being the ultimate decision makers. Accordingly, each government must answer to its own democratically elected legislature. For this reason, intergovernmental bodies 'must remain non-legal and consensual instruments. They are not a substitute for any parliament or legislature'.⁷⁶

A number of independent and effective intergovernmental bodies have proven useful when applied to a specific sector of the economy. The National Competition Council (NCC) in Australia and the Health Care Council of Canada (HCC) are examples of these types of bodies (see Exhibit 16).

EXHIBIT 16

HEALTH CARE COUNCIL OF CANADA

The Kirby Report, *The Health of Canadians – the Federal Role*, (October 2002) and the Romanow Commission on the Future of Health Care in Canada (November 2002) both identified the value of an independent council informing Canadians on health care matters while promoting accountability and transparency. The Prime Minister and the Premiers accepted the advice of those reports and Canada's First Ministers established the Health Care Council of Canada in their 2003 Accord on Health Care Renewal and enhanced its role in the 2004 Ten Year Plan.

Funded by the government of Canada, the Council reports to the Canadian public and operates as a non-profit agency. There are 26 councillors including representatives of federal, provincial and territorial governments, experts and citizen representatives. Councillors have a broad range of experience bringing perspectives from government, health care management, research and community life from across Canada. The Members of the Council are rather like a corporate board of directors, performing a liaison function between the Council and Canada's First Ministers, as well as approving the Council's budget. Supporting the work of the Health Council of Canada is a small secretariat located in Toronto.

Source: www.healthcouncilcanada.ca/en/.

Conclusion: Independence might require the following considerations, among other things:

- + Establishing a Federal Commission with an ability to determine its own work program; a funding formula to ensure 'buy-in' by all levels of government; staffed by experts from a variety of backgrounds; and a rotating chairmanship.
- + For COAG, considerations may include mandated meetings (not called by any particular level of government).



8 | INTERGOVERNMENTAL FISCAL ARRANGEMENTS

In Australia, the taxing powers of the states are limited by the Constitution and historical political circumstances. Neil Warren recently completed a report for the New South Wales Government titled *Benchmarking Australia's Intergovernmental Fiscal Arrangements*, and stated that:

The conclusion of this study is that Australia performs comparatively poorly in intergovernmental fiscal arrangements ... Australia's system of intergovernmental fiscal arrangements is characterised by very high vertical fiscal imbalance (VFI) due to inadequate State tax powers, and complex and high level equalisation.⁷⁷

Theoretically there are certain principles that can be used to assess the efficiency of the intergovernmental fiscal arrangements of a federation. Neil Warren highlights thirteen benchmarks by which to assess such arrangements. While a detailed assessment of such benchmarks are beyond the scope of this paper, a brief discussion and comparison of Australia's intergovernmental fiscal arrangements follows (although the complexity of such an analysis means that all issues will not be discussed here). Neil Warren highlights four main categories (expenditure responsibilities, tax assignment, intergovernmental fiscal transfers and dynamic federalism) that might be used to design and evaluate a fiscal system, but states in relation to such an assessment: '... the nature of the arrangements is very complex. A whole range of issues need to be taken into account when determining the appropriate mix of expenditure responsibilities, taxing powers and intergovernmental transfers where necessary.'⁷⁸

8.1 | REVENUE RAISING

In general: 'As the subsidiarity rule expresses, powers and responsibilities should be allocated to the lowest practical order of government. This applies on both the taxing and the spending sides.'⁷⁹ Ideally, this would mean that governments would have fiscal resources equal to their spending responsibilities and 'that way the government providing the benefits to the voters also inflicts the pain, and thus a measure of accountability is in operation'.⁸⁰

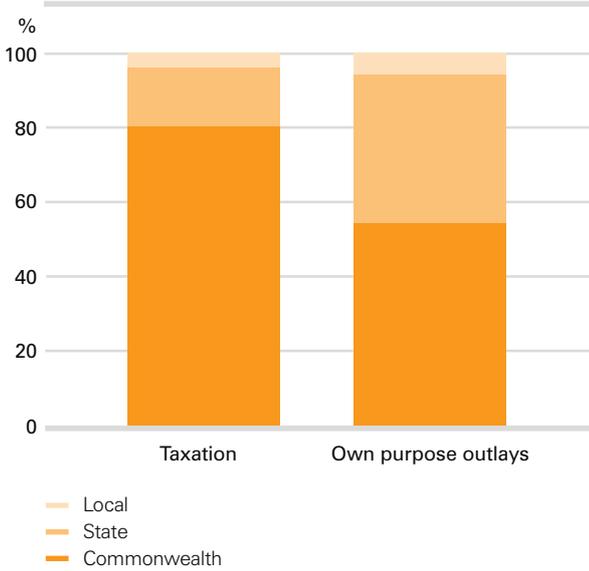
Vertical fiscal imbalance (VFI) occurs where the allocation of revenue between the federal and state governments does not match the expenditure responsibilities of those governments. VFI is measured as a ratio of the federal government's revenue (measured as a percentage of total government revenue) to its expenditure (measured as a percentage of total government expenditure).⁸¹

All federations have a degree of VFI, which has arisen from a number of circumstances including the growth in personal and corporate income tax as a source of revenue (which are generally controlled at a national level, although there is variation in the degree to which national governments dominate taxation revenue).

At one extreme lies Australia, where a high degree of fiscal centralization has funded a high degree of policy centralization. At the other extreme lie Switzerland and Canada, where revenues are more evenly balanced between national and subnational levels of government. The outlier is the EU, which ... has taken quite a different direction, one reflecting its quite different circumstances.⁸²



FIGURE 2 VERTICAL FISCAL IMBALANCE IN AUSTRALIA



Source: N Warren, *Benchmarking Australia's Intergovernmental Fiscal Arrangements*, Final Report to the New South Wales Government, May 2006, Figure 4, p. 51 (2004–2005 data).

Note: own purpose outlays include compensation of employees, use of goods and services, social benefits and other expenses, but do not include consumption of fixed capital, interest, subsidies and grants.

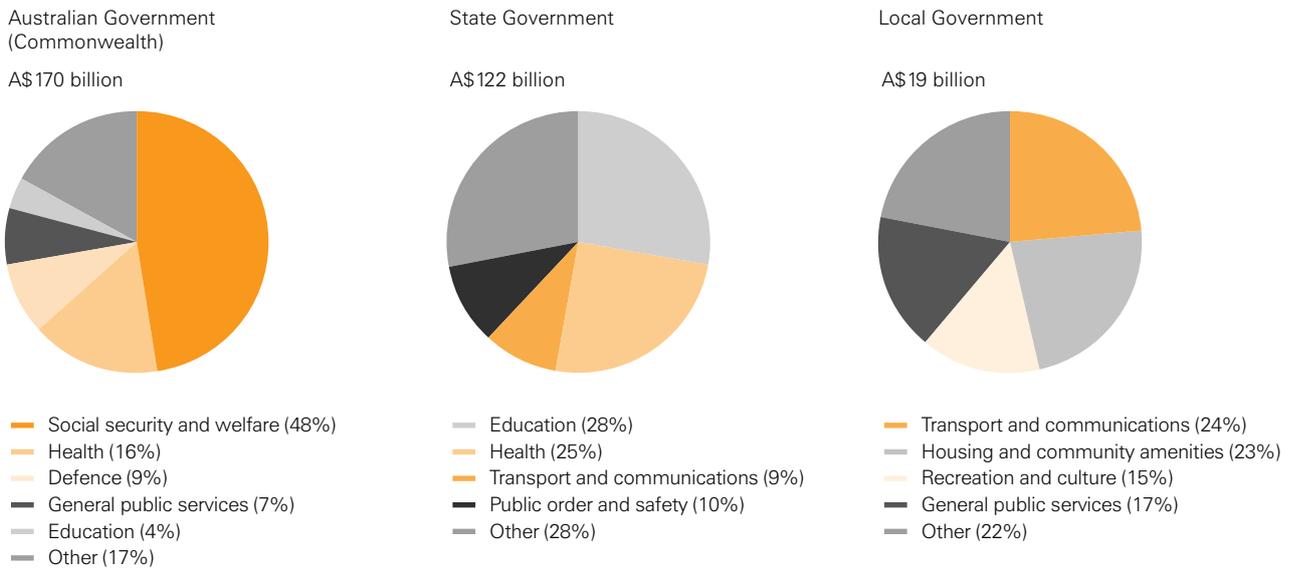
In Australia, while there is sharing of spending responsibilities in many categories (e.g. health and education) there is no sharing in taxing responsibilities. The Commonwealth has control over some of the broadest based taxes (e.g. personal and corporate income tax and customs and excises). The states, on the other hand, receive the GST (a consumption tax), for which the rates and base are set and can only be changed with agreement by all of the states, the endorsement of the Commonwealth and both Houses of Federal Parliament. The states are able to levy taxes, for example on property (e.g. rates) and payroll taxes.

Accordingly, a large vertical fiscal imbalance arises because the largest taxes are collected at the Commonwealth level, but a considerable amount of spending responsibility rests at a state (or local government) level.





FIGURE 3 **DECOMPOSITION OF PUBLIC EXPENDITURE BY FUNCTION AND GOVERNMENT LEVEL** Own purpose expenditure, 2004–05



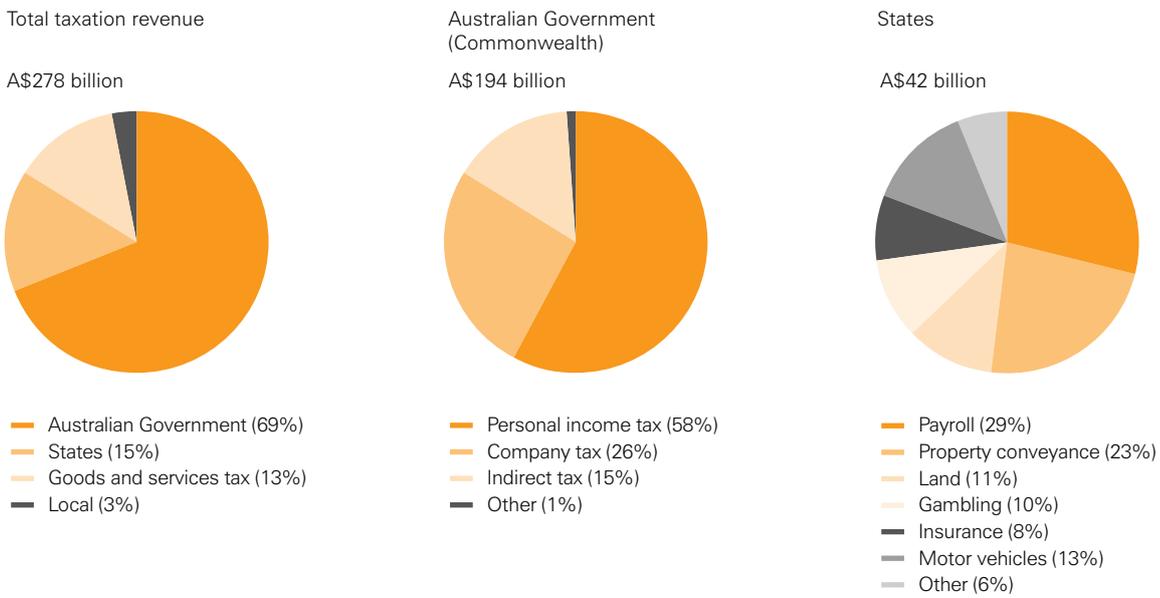
Source: OECD, *Economic Surveys: Australia*, Volume 2006/12, July 2006, p. 76 (The Treasury, Australian Government and ABS [2006], Government Finance Statistics 2004–05, cat. No. 5512.0).

Note: Australian Government excludes specific purpose payments (SPPs), state government includes SPPs to the states but excludes SPPs through the states to local government, local government includes SPPs.





FIGURE 4 **SOURCES OF TAX REVENUE** Per cent of total, 2004–05



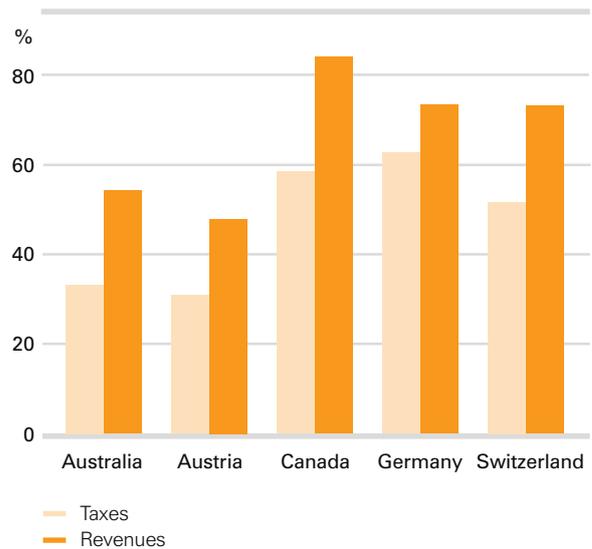
Source: OECD, *Economic Surveys: Australia*, Volume 2006/12, July 2006, p. 77 (ABS (2006), Taxation Revenue Australia (cat No.5506.0) and national authorities.

Note: All GST revenue is collected by the ATO but distributed to the states. Therefore the Australian Government revenue of 194 billion excludes GST and is excluded from the chart depicting state revenue.



VFI results in the need for the Commonwealth government to transfer funds to State governments to make up for their revenue shortfalls. The problem with such transfers is that accountability between the raising of revenue and the responsibilities for funding certain programs can become blurred. For example, the Commonwealth can avoid accountability for expenditure of funds, because the states have responsibility for a lot of the expenditure. Similarly, states can either become unable to provide certain services through lack of revenue raising capabilities, or alternatively claim they cannot provide such services due to lack of funding from the Commonwealth. States may also be less able to provide the services demanded by their electorates if much of their funding is 'tied' to conditions set out by the Commonwealth. Ensuring that revenue raising abilities and expenditure responsibilities are aligned may increase the chances of accountability for levels of governments in reaching their commitments. In Australia, there is a very high degree of VFI, which has increased over time and is one of the largest among comparable federations.

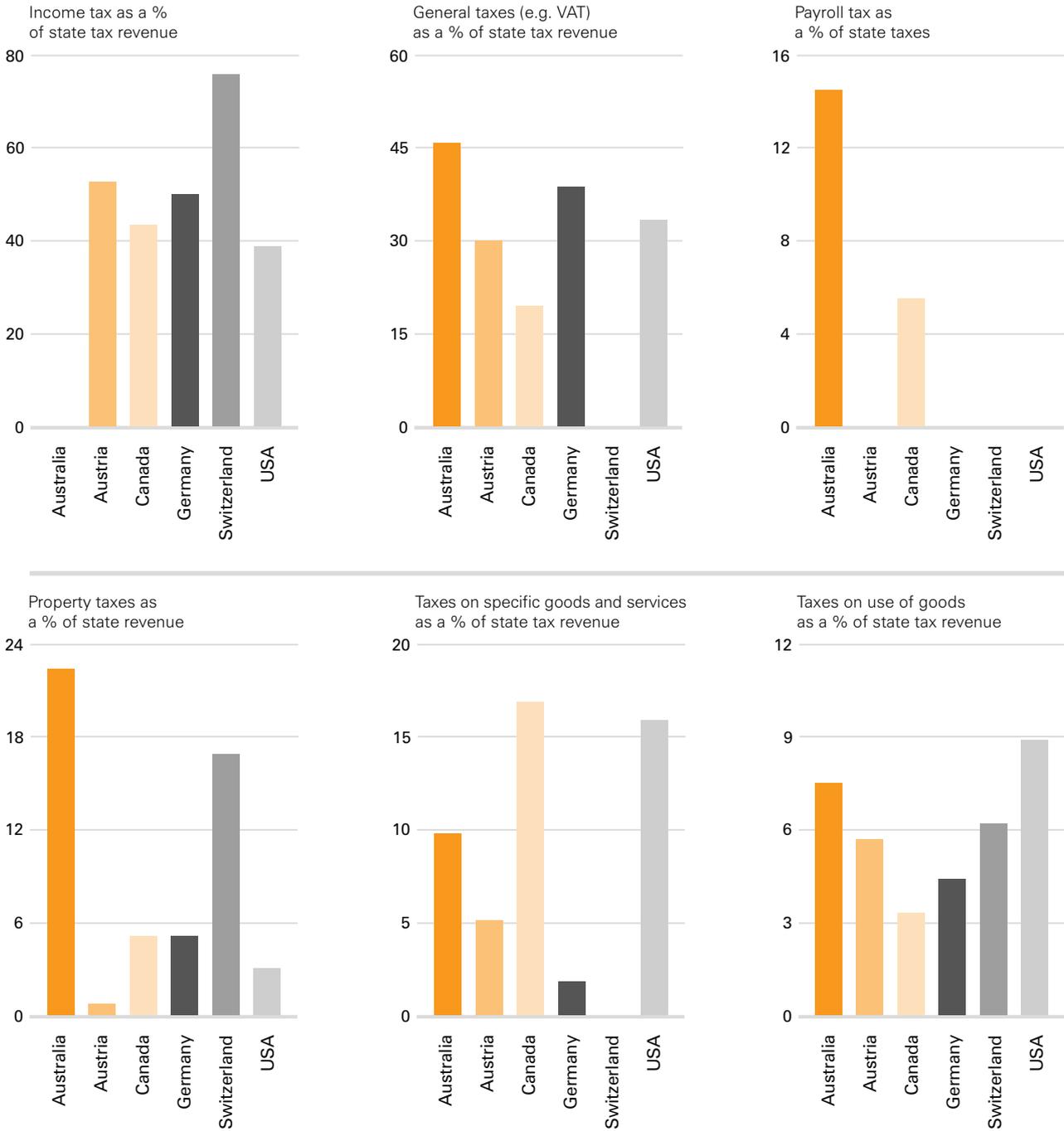
FIGURE 5 STATE GOVERNMENT OWN-SOURCE TAXES AND REVENUES AS A PROPORTION OF STATE GOVERNMENT EXPENDITURES



Source: N Warren, *Benchmarking Australia's Intergovernmental Fiscal Arrangements*, Final Report to the New South Wales Government, May 2006, Figure 8, p. 56 (Government Finance Statistics Yearbook 2004, International Monetary Fund).



FIGURE 6 STATE GOVERNMENT DEPENDENCE ON PARTICULAR TAXES



Source: N Warren, *Benchmarking Australia's Intergovernmental Fiscal Arrangements*, Final Report to the New South Wales Government, May 2006, Figure 10, pp. 65–66 (OECD Revenue Statistics 1965–2004, Table 136).



In Canada, Germany and Switzerland, the states have a greater capacity to spend from own source revenues than the states in Australia. Similarly, state governments depend to a greater extent on transfers from the Commonwealth government.

In some circumstances, it makes sense for some taxes to be collected centrally as this ensures efficiency and lowering of costs. Accordingly, the GST collected at a central level is a form of efficiency in the Australian taxation system.

As a result, it is harder to hold governments to account for the revenue raising and expenditure:

Australia represents the most acute case of VFI, with the Commonwealth controlling all major tax sources and engaging in massive annual transfers to the states. Through idiosyncratic judicial interpretation, the states have been prevented from levying their own general sales taxes and thus lack that important revenue source available to subnational governments in Canada and the United States. Through the coercive spending of the Commonwealth ... the states have been excluded since 1942 from the income tax. They were granted all the net revenue from the national value-added tax (the 'GST', Goods and Services Tax) introduced in 2000. However, that remains a Commonwealth government tax and the revenues are effectively an intergovernmental transfer. The Australian states rely on transfers for almost half their entire budgetary needs.⁸³

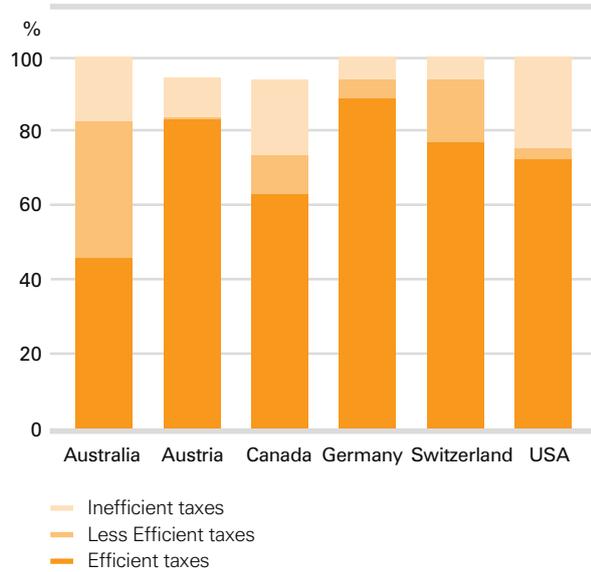




However, the flexibility for states to impose taxes is limited, and often limited to inefficient taxes, which will ultimately place a cost burden on the economy. Because the states lack access to the most efficient sources of taxation, this limits their ability to increase their revenue in a manner that will not increase the cost burden to the economy:

A further simplification which should be considered would involve broadening the GST base. Revenue from this measure could be used to reduce the direct tax burden on labour and further address the vertical fiscal imbalance. However, such a change in the tax base would require the agreement of all state governments and would also require significant changes to the financial arrangements between the federal and state governments.⁸⁴

FIGURE 7 PROPORTION OF STATE GOVERNMENT TAX REVENUE FROM EFFICIENT SOURCES



Source: N Warren, *Benchmarking Australia's Intergovernmental Fiscal Arrangements*, Final Report to the New South Wales Government, May 2006, Figure 11, p. 67 (OECD Revenue Statistics 1965–2004, Table 136).

Note: taxes include taxes on incomes and profits, payroll taxes, property taxes, general taxes (e.g. VAT), taxes on specific goods & services, taxes on use of goods and 'other taxes'. 'Other taxes' have not been included in Figure 7 so Austrian and Canadian taxes do not sum to 100 per cent.



Neil Warren writes in relation to the states' revenue raising efficiency:

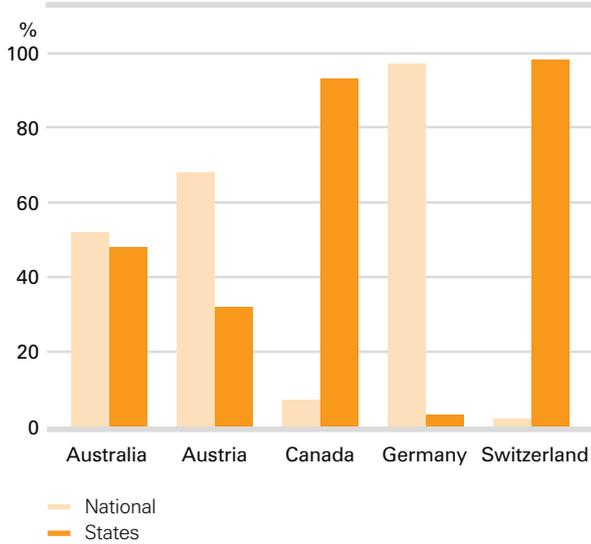
Australian states rely on efficient taxes for a smaller proportion of their tax revenue than other federations ... The result would look even worse if the GST was not included as a State tax by the OECD, from which the data in [the figure above] is drawn.⁸⁵

There are methods of overcoming or altering this centralising trend. This has been seen in some overseas jurisdictions like Canada, where the taxing powers were restored to the provinces over time and the conditionality on the remaining transfers was reduced. 'By the late 1990s, provincial reliance on cash transfers had been almost halved to 13 per cent of their total expenditures.'⁸⁶ Other countries have also been reviewing and undertaking reforms in relation to their fiscal relations. In Italy, for example, the regions have been assigned new taxing powers and a new system of interregional transfers has been developed (this process of reform is as yet incomplete).⁸⁷

8.2 | SPENDING

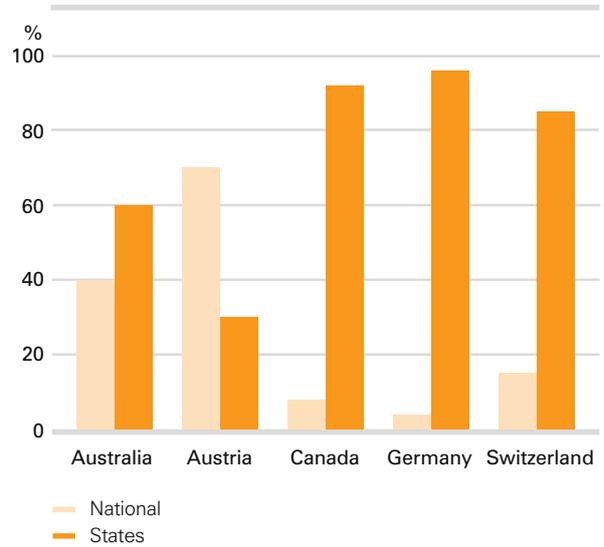
There is a pattern of spending responsibilities across federations (with some exceptions). In general, Australia differs from other federations in relation to health and education spending, and this therefore increases the likelihood of policy duplication and blame shifting in those areas that are shared.⁸⁸ However, even those shared responsibilities that are commonly shared among federations (e.g. economic affairs, housing and community amenities) will have the risk of lack of accountability if appropriate fiscal and coordination mechanisms are not properly considered.

FIGURE 8 HEALTH EXPENDITURE –
CENTRAL GOVERNMENT V STATE GOVERNMENT



Source: N Warren, *Benchmarking Australia's Intergovernmental Fiscal Arrangements*, Final Report to the New South Wales Government, May 2006, Figure 1, p. 37 (Government Finance Statistics Yearbook 2004, International Monetary Fund).

FIGURE 9 EDUCATION EXPENDITURE –
CENTRAL GOVERNMENT V STATE GOVERNMENT



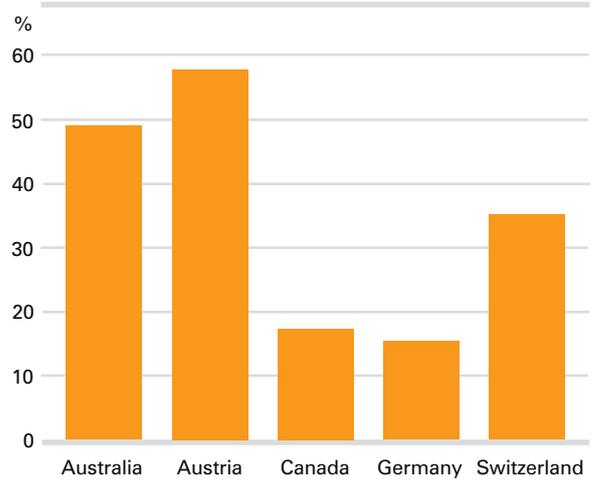
Source: N Warren, *Benchmarking Australia's Intergovernmental Fiscal Arrangements*, Final Report to the New South Wales Government, May 2006, Figure 2, p. 37 (Government Finance Statistics Yearbook 2004, International Monetary Fund)



While there are a number of federations that have shared spending responsibilities between levels of government in certain areas of the economy, the 'lack of transparency appears to be less problematic where State governments have relatively high levels of fiscal autonomy, as in Canada and the USA.'⁸⁹

In Australia, GST revenues collected by the Commonwealth are automatically provided as revenues to the states.⁹⁰ However, there is a comparatively high degree of other transfers from the Commonwealth to the states in Australia as well.

FIGURE 10 TRANSFERS AS A PROPORTION OF STATE GOVERNMENT EXPENDITURE



Source: N Warren, *Benchmarking Australia's Intergovernmental Fiscal Arrangements*, Final Report to the New South Wales Government, May 2006, Figure 9, p. 57 (Government Finance Statistics Yearbook 2004, International Monetary Fund).





Section 96 of the Constitution allows the Commonwealth to 'grant financial assistance to any State on such terms and conditions as the Parliament sees fit.' These transfers are commonly known as conditional grants or Special Purpose Payments (SPPs).

Conditional grants have become commonly used in federations and have led to a major centralising trend. 'Those who pay the piper call the tune in federal systems as elsewhere. The stronger fiscal position of central governments has proven a tempting and powerful lever for the extension of central government power into areas of subnational jurisdiction.'⁹¹ In Australia, SPPs to the states make up about 13% of Commonwealth expenditure, and include areas that are traditionally the spending responsibility of the states (e.g. health and education).

Section 96 of the Constitution has been given broad interpretation by the courts and the High Court, which 'has interpreted this as precluding any possible limitations on the conditions that the Commonwealth imposes on state governments through the spending power. Indeed, it has endorsed the use of the spending power as a weapon to exclude the states from access to the kind of tax bases that would reduce their dependence on such grants.'⁹² For example, the High Court upheld the ability of the federal government to make grants to the states contingent on the states agreeing not to impose income tax, and banning state sales taxes.

Therefore, giving the states access to greater taxing powers (e.g. allowing a broader GST taxation base) may have the effect of reducing SPPs from the Commonwealth Government to the states.

In Spain, there has been a process of reform whereby healthcare and social services spending has been assigned to Autonomous Communities. France has also undergone a reform process whereby public functions such as higher education, industrial policy and regional infrastructure have been decentralised (constitutional reform of 2003).⁹³ In Germany, an expert panel has been established to consider the allocation of responsibilities in the federal system.⁹⁴

A simpler system of inter-governmental transfers involving so-called 'specific-purpose payments' would contribute to a clearer specification of spending responsibilities. The specific-purpose payments should become less complex and inflexible. A first step would be to develop an outcome/output performance and reporting framework for each SPP. This is an ambitious task as outcome/output measures of service delivery are difficult to clearly define, measure and enforce in a robust way. Nevertheless, such frameworks could ultimately lead to a move towards the funding of such payments on an outcome/output basis in certain areas, such as education.⁹⁵

The OECD notes, however, that the UK experience shows that outcome-focused performance targets should be clear. Those targets should be simple to quantify and audit (and should be tied to financial incentives such as the competition payments that proved useful in the NCP reforms).



8.3 | FISCAL EQUALISATION

It is common among federations around the world for the national government to distribute funds to the states (as previously discussed), and it is also common for equalisation across states to occur. Horizontal Fiscal Equalisation (HFE) occurs when funds are transferred from one subnational region to another to ensure that some form of uniformity of service provision occurs.

In Australia, compared to some other federations such as Canada and Switzerland, there is no reference to HFE in the Constitution. However, even though there is no reference to HFE, Australia has a complex system of HFE. In fact, Australia employs a system that attempts to fully equalise the revenue-raising capacity and expenditure needs of the states, even though it has one of the lowest pre-equalisation fiscal disparities.⁹⁶

In Australia, VFI and HFE are integrated, with the large volume of Commonwealth transfers (including GST revenues) being divided among the states according to the equalization formula. Since 1993, an autonomous agency, the Commonwealth Grants Commission, has had statutory responsibility for those allocations ...⁹⁷

There are a number of different examples of equalisation formulas employed across jurisdictions, each with their own characteristics (and benefits and pitfalls). For example, in Australia the complex equalisation formula ensures that weaker states are 'brought up to the national average' and that 'stronger states are bought down'.⁹⁸ In Germany, equalisation is almost 'punitive' in character, given that surplus revenues are distributed directly from affluent to poorer Länder.⁹⁹ This has led to some criticism of the equalisation program in Germany, as it is suggested that it removes the incentives for Länder to perform well or improve their performance. In contrast, in Canada the richest state (Alberta) is excluded from the calculation of the national average, which means that the poorer states are brought 'up to the adjusted average without bringing the richer ones (Ontario and Alberta) down'.¹⁰⁰

At the other extreme, the United States practices very little systematic equalisation (which may arise from the historical formation of the federation and the presidential system of government).¹⁰¹

There are differing views on the efficacy of fiscal equalisation, particularly as such a practice modifies market outcomes. For example, some argue that subnational governments lose the incentive to improve their performance if equalisation practices diminish the costs and benefits of the market outcomes and signals. 'Most fiscal equalisation methodologies in comparator federations are significantly less complex and more transparent than in Australia.'¹⁰²



8.4 | MONITORING

It is important for countries to assess their intergovernmental fiscal arrangements on a regular basis. Over time revenue raising and expenditure responsibilities in federal systems evolve, often on an ad hoc basis and relating to changes in the local economy and global environment. Whether the intergovernmental fiscal arrangements are optimal requires an assessment across the board of the fiscal arrangements.

Changing circumstances have meant that the original intentions of founders of federations may not fit with a modern economy because: 'The classic legislative federations were established in an altogether different era when the size and scope of government were limited, and it was relatively easy to divide responsibilities and to imagine two levels of government operating in their own spheres with little clash or overlap ... The 'mixed economy', the welfare state, the rise of environmental policy, and the enormous increase in taxation have all greatly complicated policy making in a system of divided jurisdiction – as have the vastly greater mobility of labour, geographical scope of economic activity, and quality of communication and transportation.¹⁰³

Many other countries have undergone assessments of their fiscal arrangements:

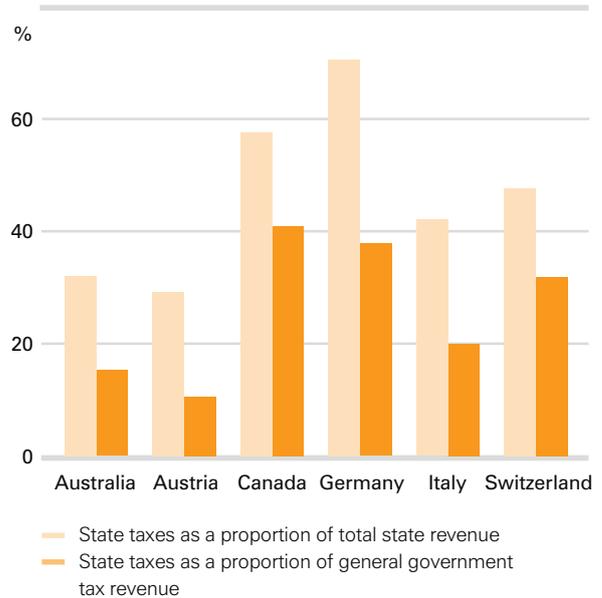
Australia needs to reconsider the allocation of expenditure responsibilities between levels of government, and the consequent assignment of tax bases and intergovernmental financial transfers. Over recent years, Belgium, Germany and Switzerland have all significantly revised their federal arrangements. Reforms are underway in Italy, and Austria comprehensively reviews its intergovernmental arrangements every four years.¹⁰⁴

8.5 | POLICY

What is clear is that there are a variety of potential models of fiscal federalism that may be employed in Australia, and many examples of different methods from overseas. Furthermore, there is little constitutional constraint on what might be done from a fiscal perspective. The arrangements that are currently in place have arisen over time from historical circumstances. Australian states have comparatively low levels of fiscal autonomy compared with overseas countries. Perhaps a comprehensive review of intergovernmental fiscal arrangements and comparative analysis with overseas models may yield some insights into what might be a more optimal arrangement.

One level of government may have the constitutional authority but not the fiscal resources or ability to contain spillovers, while the other level of government may have the resources and reach but no the requisite authority.¹⁰⁵

FIGURE 11 MEASURES OF FISCAL AUTONOMY



Source: N Warren, *Benchmarking Australia's Intergovernmental Fiscal Arrangements*, Final Report to the New South Wales Government, May 2006, Figure 12, p. 73 (Government Finance Statistics Yearbook 2004, International Monetary Fund; note data not available for USA).



What is clear is that if the subnational governments are given more taxing responsibilities, then accountability must also be assured through a process of adequate assignment of responsibilities.

With regard to the revision of subnational government financing systems, the reforms pursued have the general aim of improving decentralised governments' accountability, by assigning them more tax autonomy and by providing more flexibility in the use of central government financial transfers. In Italy, Spain and France decentralisation has been coupled with the assignment of new taxing powers to subnational governments.¹⁰⁶



9 | CONCLUSION

There are a number of themes arising from this international comparison of intergovernmental arrangements that could provide examples of practical solutions in the Australian context. In summary, some of the considerations could include:

- + **A formal institutional arrangement or mechanism** – a permanent independent intergovernmental body at a federal–state level (e.g. formal institutionalisation of COAG) as well as a permanent independent policy body (in this paper called the Federal Commission). Such formalisation could be through a scheme of cross-jurisdictional uniform legislation or by formal agreement.
- + **Administrative mechanisms to facilitate decision making** – including the establishment of a permanent intergovernmental Secretariat to provide administrative and policy support (to the CRC, the Federal Commission and COAG); an independent and rotating chair; sufficient resources (e.g. staff). Other considerations are whether there should be consensus or majority voting mechanisms within the decision-making bodies, the funding of both the Secretariat and the Federal Commission and the role of the Secretariat (e.g. research and agenda setting).
- + **Flexibility to determine innovative solutions** – a sound ‘theoretical’ framework and basis for decision making (for example, mandated principles of federalism/goal setting as a framework for dividing responsibilities may be one method as a basis for decision making).
- + **Transparency** – for example, if a Federal Commission were established it could provide independent and publicly available reports to COAG on policy items. Such a report could make recommendations that would put pressure on all governments to consider the issues. Further, if a Secretariat were established then publicly available agendas and preparatory material could be developed prior to any meeting of COAG (agendas must flow from one meeting to another) – this would enable public discussion of policy items prior to the meetings.
- + **Accountability** – achieved by ensuring that an independent body to do research on policy issues is established – called a Federal Commission in this paper (see discussion in ‘Independence’). The Federal Commission should have a clearly publicised charter (e.g. its make-up and objectives and role). The outputs of the Federal Commission should also be made public.
- + **Efficiency** – there must be an agreed number of meetings of COAG per year (e.g. at least 2 per annum) as well as agreement that COAG will respond to the recommendations of the Federal Commission in a given time frame.
- + **Independence** – the Federal Commission should have the ability to determine its own work program, a funding formula to ensure ‘buy-in’ by all levels of government, staffed by experts from a variety of backgrounds and a rotating chairmanship.
- + **Review of federal fiscal arrangements** – a review of fiscal arrangements should be undertaken to obtain a greater degree of responsibility and transparency about which level of government is responsible for delivering outcomes in which policy areas. Comparisons with overseas countries reveal that reform of fiscal arrangements is possible and has been undertaken overseas.

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