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Australian Journal of Political Science

Publication details, including instructions for authors and subscription information:
<http://www.informaworld.com/smpp/title~content=t713404457>

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To cite this Article: Parkin, Andrew and Anderson, Geoff , 'The Howard Government, Regulatory Federalism and the Transformation of Commonwealth-State Relations', Australian Journal of Political Science, 42:2, 295 - 314

To link to this article: DOI: 10.1080/10361140701320034

URL: <http://dx.doi.org/10.1080/10361140701320034>

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The Howard Government, Regulatory Federalism and the Transformation of Commonwealth–State Relations

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Various initiatives enhancing Commonwealth power relative to the States have been a feature of the Howard government that has surprised many observers. These developments need to be understood in the context of longer-term political, financial and regulatory changes that are challenging established features of Commonwealth–State relations. The Howard government's allocation of Goods and Services Tax (GST) revenue has offered the prospect of greater State-level financial and policy autonomy. But the Howard government has also inherited, and in some policy domains has significantly enhanced, the further development of a Commonwealth–State regime best described as 'regulatory federalism'. Its effect, in contrast to the effect of the GST initiative, is to constrain the States' scope for policy autonomy. A similar impact is emerging from the Commonwealth's efforts to ensure that its conditional grants to the States better serve Commonwealth policy goals and priorities. And a raft of Commonwealth initiatives is bypassing the States altogether. Although the Howard government has clearly enhanced the role of the Commonwealth, it remains constrained by aspects of the federal system that are structurally entrenched and that continue to make intergovernmental collaboration, rather than confrontation, a sensible strategy.

A transformative engagement with Commonwealth–State relations has been among the Howard government's most significant but least expected activities. Prognosticators looking ahead in March 1996 might well have predicted that a long-surviving Howard government would leave a significant impression in a number of policy domains: industrial relations, taxation, foreign relations, trade, privatisation and some other well-signalled interests. But a re-alignment of Commonwealth–State relations was not an obvious future focus.

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It has only been relatively recently, in the past couple of years of the Howard government's first 10 years in office, that analysts—in journalism or in academe—seem to have noticed the significance of the government's actions for the federal system.¹ Such inattention is understandable. The Prime Minister and various key members of his government have begun to articulate an explicit 'new nationalist' position only relatively recently, a timing that is probably not unconnected to the fortuitous post-2002 partisan configuration of a Labor monopoly on government in all of the States and Territories. And the shift in some policy domains towards an unapologetically enhanced Commonwealth stance does stand in interesting contrast to probably the biggest single impact of the Howard government on the role and capacity of the States: the creation from July 2000 of the 'new tax system' with its automatic flow of all Goods and Services Tax (GST) revenues to the States. The GST flow has strengthened the long-term position of the States.

This article argues that the Howard government has now clearly moved towards championing a more dominant and directive Commonwealth government. This new trajectory is assisted by some longer-term structural shifts in the architecture of Commonwealth–State relations. But it remains constrained by other aspects of the federal system that are structurally entrenched that continue to make sensible intergovernmental collaboration, rather than confrontation, a prudent strategy even for ambitious Commonwealth governments.

The paper identifies four dimensions to the trajectory of Commonwealth–State relations in the Howard period.

- *Fiscal federalism*: The post-GST system of fiscal federalism is a positive development for the States but, nonetheless, it encompasses ambiguities and uncertainties that can work in the Commonwealth's favour.
- *Regulatory federalism*: The Howard government inherited—and has enhanced—a structurally rebalanced set of Commonwealth–State relations, the origins of which date principally from the Keating Labor governments of 1993–96, although with deeper roots in a century of intergovernmental evolution. A system has been revealed that is best described as 'regulatory federalism'. The States resemble regulated agencies operating, with varying degrees of collaboration or friction, within Commonwealth-dominated clusters of regulatory regimes.
- *Program federalism*: Within the realm of Commonwealth-funded 'tied grant' State programs, a strategy of trying to re-engineer program oversight arrangements to facilitate the better fulfilment of Commonwealth goals can be detected almost from the very beginning of the Howard government's tenure in 1996. Ten years of the Howard government have refined what now seems to be a much stronger system of Commonwealth oversight of and prioritisation within State-delivered programs.
- *Parallel federalism*: There is a growing incidence of unilateral action by the Commonwealth that bypasses, marginalises or directly overlaps with the States in areas long considered to be within their jurisdictional and program responsibilities.

This paper reviews these four dimensions of the transformation of Commonwealth–State relations in the Howard era.

¹A notable exception is Jenny Stewart's prescient analysis of the first Howard government (1996–98) in terms of 'a de-emphasising is not a reversal' of the Liberal Party's customary championing of federalism (Stewart 2000, 151).

Fiscal Federalism: The GST Revolution

The Howard government's 'new tax system', with the GST as its centrepiece, has produced a landmark shift in fiscal federalism.² It is the single, most important reform to Commonwealth-State financial relations since the imposition of uniform national income tax in 1942.

From a States' perspective, the financial story of the twentieth century had been the erosion of their financial independence and the rise of the Commonwealth to uncontested dominance of the public finance system (Galligan 1995, Ch. 9; Parkin 2003; Summers 2006). The States had entered the Australian federation in 1901 as self-funding, as well as self-governing, but a structural disparity between the revenue-raising capacities and the expenditure needs of the two tiers of government—'vertical fiscal imbalance'—soon became apparent. Within a relatively short period of time, some States were needing, and receiving, Commonwealth financial assistance. Coordinated governmental borrowing activity, as formalised in 1927 and given constitutional status in 1928 via the Loan Council, likewise, became Commonwealth-controlled.³ Then Commonwealth financial dominance was truly cemented by its monopolisation of income tax collection during the 1940s.

This all set in place what became a familiar annual financial cycle. The Commonwealth collected all income tax. It then 'reimbursed' funds back to the States, in the form of unconditional general revenue grants (known as Financial Assistance Grants), as compensation for the revenue that the States had lost through the discontinuation of their former income tax programs. Other Commonwealth funds (an increasing proportion over time) were disbursed to the States in the form of conditional grants for specific programs (known as Special Purpose Payments).

The politics of this also became well established. There was an annual Premiers' Conference at which the Commonwealth made a financial offer to the States. The offer, notwithstanding the protestations of those who remembered the original 'reimbursement' rationale for the system, was a product of the Commonwealth's assessment of what was economically and politically appropriate. The States periodically lobbied for a return to some sort of automatic access to a 'growth tax'—a tax producing a substantial revenue yield linked to economic activity rather than to a Commonwealth-level governmental decision—but these wishes and efforts came to nothing.

In the early years of the Howard government, vertical fiscal imbalance was exacerbated by High Court decisions declaring long-established State licensing fees (which extracted revenue from the sale of tobacco, alcohol and petrol) to be excise duties available (under Section 90 of the Constitution) exclusively to the Commonwealth (James 1997). This necessitated an awkward scramble in which the Howard government agreed to collect these revenues for the States.

The implementation of the new GST from July 2000 radically changed the fiscal relationship between the Commonwealth and the States by channelling all of the GST

²On the Howard government's broader tax reform agenda, of which the post-2000 'new tax system' has been a major feature, see Daly (2005) and Fenna (2006).

³The Loan Council continued in something like this form for the next 60 years or so. When the Loan Council arrangements were liberalised in the 1980s so that the States, once again, became direct borrowers on world capital markets, they were not liberated from the need for a blessing from a superior authority: its locus arguably just shifted from the Commonwealth to the international credit-rating agencies.

revenues to the States. This arrangement was not part of the original policy rationale for the 'new tax system'. The Howard government's case for tax reform was based mainly on a claimed need for a rebalancing between indirect consumption taxes and direct income taxes (Fenna 2006). Using the GST to replace the unconditional Commonwealth grant to the States was a masterly piece of policy design.

Politically, it split the Labor camp. It separated the then State Labor Premiers (Carr in NSW, Beattie in Queensland, and Bacon in Tasmania) from Federal Labor's strident opposition to the GST. The Labor Premiers were permitted to record their 'in principle' opposition to the GST within the Intergovernmental Agreement, but their supportive informal comments elsewhere were not difficult to interpret.⁴

Politics aside, the GST arrangement was a significant development structurally and philosophically. It gave the States access to the economy-linked 'growth tax' so long craved. Overnight, it abolished the need for Premiers' Conferences, tossing what had seemed to be an entrenched annual political ritual—Premiers waiting in turn to express outrage, for the benefit of back-home TV coverage, at the Commonwealth's wicked parsimony—into the dustbin of history. Prime Minister Howard is on firm ground in claiming that 'with the GST, my Government delivered the most important federalist breakthrough since the Commonwealth took over income taxing powers during World War II. . . . No [Commonwealth] government in 60 years has given the States more fiscal autonomy to fulfil their constitutional responsibilities' (Howard 2005).

Although it has taken a few years for the new system to be fully phased in, the Commonwealth has guaranteed that no State would be worse off during the phase-in period, and it seems generally agreed that the eventual financial transfer to the States has been, and will continue to be, greater than would have otherwise prevailed. Crucially, the financial payment is harvested directly from national economic activity rather than being dependent on Commonwealth fiscal policy decisions.

It all adds up to a genuinely pro-federalist initiative, consistent with the pro-federalist stance that commentators and analysts have long assumed to be predominant within Liberal Party thinking.⁵ This conclusion is reinforced, rather than undermined, by some later expressions of regret—reflecting a more centralist policy and fiscal agenda—emanating, in particular, from Treasurer Peter Costello.

I think, as you look back on it, the most generous aspect of our tax reforms was the allocation of GST revenues to the [S]tates—untied. The object of doing that was to essentially give the [S]tates a revenue base for which they would take responsibility and out of which they would accept their expenditure obligations.

It hasn't happened, and you would have to say that element was a failure.

The fundamentals changed but the states never changed the script. I think this is one area, the most generous and one of the most fundamental changes, the allocation of a growth tax to the [S]tates, which has not proved successful. (Costello interviewed by Shanahan 2006)

⁴Premier Carr: 'I have got to say that I have never been at a more successful Premiers' Conference in the four years I have been in this job. . . . It does represent a transformation. It is the national government handing over a growth tax that is going to be the basis for State revenues from now on in.' Premier Beattie: 'Queensland, if the GST goes through, . . . will be better off.' Premier Bacon: 'I am the first Tasmanian leader to go to Canberra and come away not worse off.' (Government Senators 1999)

⁵For discussion on this—fairly recent but predating the more transparent centralism of the latter Howard years—see Sharman (2001) and Norton (2004, 27).

But this historic shift in fiscal federalism is not necessarily without complications and pitfalls for the States. Technically, the advent of the GST has exacerbated rather than reduced 'vertical fiscal imbalance' (VFI). This is because, despite the Howard government's attempt to disown it in statistical compilations (probably in order to deflect criticism that it had become a 'high-tax government'), the GST remains a Commonwealth tax.⁶ And under the Intergovernmental Agreement of April 1999, ratified in final form in June 1999, the States agreed—in return for signing on to the GST money flow—to abolish or reduce some State taxes, including financial institutions duties, stamp duties on share trading and debits taxes. Hamill (2005, 306–7), although acknowledging that the reforms have produced an enhanced State-level 'budgetary capacity', argues that the eroded State-level 'fiscal capacity' producing the exacerbated VFI constitutes 'yet another manifestation of...creeping centralisation'.

More worrying from a State perspective have been the periodic reminders from Treasurer Costello that the new arrangements have not entirely removed the Commonwealth's ability to irritate the States in relation to unconditional grants. These reminders have been accompanied by unnerving hints that the unconditional GST disbursement may not necessarily operate permanently. It was Costello who pointedly reminded the States—most notably at the March 2005 Treasury Ministers' Conference—that the Intergovernmental Agreement obliged them 'by 2005' to 'review the need for the retention' of a list of additional State-imposed duties (Commonwealth and States 1999). Costello's preferred interpretation of this seems to have been that the States had (explicitly or implicitly) agreed to move towards full abolition of these taxes. State leaders simply quoted back their obligation merely to 'review the need for the retention' of the duties. Behind the exchange was an implied threat to the longevity of the Agreement and a further implied threat that, in any case, the Commonwealth had other ways—such as through cut-backs in Special Purpose Payments—to punish non-compliant States. Tellingly, all the States in due course (New South Wales and Western Australian most reluctantly) proceeded to announce an abolition or phase-down of the kind of duties to which Costello was referring.

Overall, the GST reform has unquestionably served to strengthen, for now at least, the financial position of the States,⁷ but Costello has revealed that a Canberra hook might still be attached to the GST lure.

⁶This led to the curious situation of some Commonwealth agencies—the Departments of Treasury and Finance (see, for example, Department of Treasury 2003)—dutifully following the political preferences of their Ministers by reporting the GST as a State tax, and other Commonwealth agencies—the Australian Bureau of Statistics, (see, for example, ABS 2000)—showing their professional independence by correctly reporting the GST as a Commonwealth tax.

⁷Not analysed here—because it is more of a State-State than a Commonwealth-State issue—is the occasional continuing friction over the 'horizontal fiscal equalisation' that continues to structure how the Commonwealth's unconditional allocation to the States is distributed between them. This continues to be determined, as it has since 1933, via the recommendations of the Grants Commission. Since the advent of the GST—perhaps because it is now relatively easy to compare a particular State's contribution to overall GST revenue with the share that its government receives from the Commonwealth, the complaints from the 'donor' states—notably New South Wales and Victoria—have become more frequent (Wilkinson 2003; Warren 2006). One effect of the GST arrangements has been to subject the Grants Commission equalising process a greater proportion of Commonwealth payments to the States (Collins 2004, 6; Warren 2006, xxii). The system looks entrenched for at least the foreseeable future.

Costello's remarks are a reminder of the other dimensions of the Howard government's relationships with the States to which this article now turns. These other dimensions have had a decidedly, and surprisingly, centralist orientation. Some elements only came into clear focus after several terms of the Howard government, perhaps provoked in part by Costello-type post-GST second thoughts or perhaps by the post-2002 coincidence of a Commonwealth Coalition government facing a uniform pack of Labor-controlled States and Territories. Other elements can be detected from the very start of the Howard period in government.

Regulatory Federalism: Building on the Inheritance

Bequeathed to the incoming Howard government in March 1996 was an evolving system of Commonwealth–State relations that can be usefully described as *regulatory federalism*.

Regulation uses rules, regimes and incentive structures to shape the behaviour of actors.⁸ Regulation has become an increasingly prominent mode of governance, as notions of public-sector ownership and governmental command give way—via privatisation, outsourcing, downsizing, consultation, devolution, regionalisation, competition, contestability and other related public-sector changes—to more negotiated, contractual and networked relationships between the public, private and non-profit sectors. These relationships can be understood as constituting regulatory regimens—some quite formalised, others less so but regulatory, nonetheless.

Australia's federal system has arguably constituted a special case of a regulatory regime—although not labelled as such—from the beginning. Its intergovernmental relationships have never, for constitutional and political reasons, been based principally on hierarchy, command or control. Rather, the history of Australian intergovernmental relations reveals changing patterns of negotiation, rule setting and networking, using a range of incentive structures. In short, it has been a history of evolving regulatory structures.

Some of the longstanding regulatory structures have been quite formalised and predictable—at the macro level via Premiers' Conferences, Grants Commission determinations and other such devices, and at the sectoral or program level via formal agreements.⁹ Sometimes the regulatory structures have been less formalised. Since the mid 1990s, more policy sectors have been moving to identifiable formal regulatory arrangements. This has been the most enduring outcome of the (mostly) cooperative 'new federalism' initiatives begun in 1990 under the Hawke government (Parkin 1996b; Painter 1998) and—exemplified by National Competition Policy and embodied by the Council of Australian Governments¹⁰—continued in spirit and practice under the Keating and Howard governments.

⁸For various perspectives on regulation as a mode of governance, see Head and McCoy (1991), Gow and Maher (1994), Majone (1997), Black (2002), Braithwaite (2002, Ch. 2), Hollander (2002) and Grant (2005).

⁹A good example is the longstanding Commonwealth–State Housing Agreement (Parkin 1992; Caulfield 2000).

¹⁰Council of Australian Governments comprises the Prime Minister, the six State Premiers, the two Territory Chief Ministers and the President of the Australian Local Government Association (Parkin 2007a).

National Competition Policy

The special significance of the National Competition Policy (NCP) Agreement of April 1995, negotiated under the Keating Labor government but soon operating under the ambit of the Howard Coalition government, must be emphasised.¹¹

The declared purpose of the NCP agreement was to facilitate microeconomic reform by creating and extending national competitive markets for goods and services. The ambit from the start included enterprises, such as utilities, which had long been under State monopoly control. The States agreed to a new competitive regime in return for substantial Commonwealth financial payments (in recognition that reform was likely to produce greater Commonwealth tax revenues but lower internal budgetary returns to the States). The regime was overseen until 2006 by a National Competition Council.

Among the impacts of NCP has been a transformation—via privatisation, corporatisation, disaggregation and other structural changes—of the big State-owned utilities. The NCP has also reached into the State management of a host of other areas.

Take Tasmania as an example. In 2001, the Tasmanian State government reported that, as a direct consequence of NCP compliance requirements, it had amended or repealed 124 of its Acts. It had been forced to review and reform, in conformity with the principles of competitive neutrality, a host of its key services and authorities, including taxi licensing, car safety, retail trading hours, regulation of the legal profession, electricity competition, mineral exploration regulation, liquor licensing, motor accident insurance, water supply arrangements, ports management, public transport, dairy regulation, student housing, ambulance services and public swimming pools (Tasmania Treasury 2001).

These policy domains are complex arenas shaped by a variety of arguments, values and interests, many of them contentious. For example, there can be genuine disagreement about the most appropriate way for the public sector to regulate the sale and consumption of alcoholic beverages, or about the degree to which there should be governmental control over shop trading hours. In the past, these disagreements have been debated and resolutions reached within the arena of State politics, with the outcomes embodied in State legislation and State administrative practices. The NCP made these local political resolutions subordinate to a regulatory regime beyond the reach of State politics (and, incidentally, a regime that by its nature is suspicious of governmental controls per se and more enamoured of competitive private-sector markets). The fact that elected members of democratically-constituted bicameral State Parliaments might have views about the appropriateness of some of these changes and refuse to pass enabling legislation has not impressed the National Competition Council. Western Australia was penalised by the withholding of NCP payments, notwithstanding that its failure to reform retail trading hours was the result of WA voters in February 2005 defeating an enabling referendum on the issue (Bennett 2005).

Whatever their intrinsic merits, NCP-compliant reforms have reduced the scope for discretionary action by States. The reforms may arguably serve the putative national interest in some sense, although this would be contested by some observers, but they do not necessarily serve the interests of any particular individual State. And

¹¹On National Competition Policy, see Griffin, Svensen and Teicher (1999), Argy (2002), King (2003), Kain, Kuruppu and Billing (2003), Hollander (2006).

it can be difficult under these circumstances for the States to make the obvious, but infrequently appreciated, point that the national interest is not necessarily synonymous with the interests of the Commonwealth government.¹²

It is extraordinary to observe that, with the consent of the States, NCP put in place a national regulatory framework not principally for *inter*-governmental or *multi*-governmental activities but rather for significant *intra*-governmental activities. The effect has been to interpose national-level policy and program priorities into areas within State constitutional jurisdiction.

Council of Australian Governments

Council of Australian Governments (COAG) was formally constituted in 1992, institutionalising what had been a series of ad hoc Special Premiers' Conferences that began in October 1990 (Parkin 2007b). Beyond the special NCP initiatives, COAG oversaw the development of new collaborative arrangements—creating new regulatory regimes—that began to provide coordinated national governance over such matters as interstate road transport, the rail network, companies and securities regulation, uniform credit laws, food standards, vocational education and training standards, non-bank financial institutions; and the 'mutual recognition' across all States of standards, licences and qualifications awarded in any particular State. These new arrangements are by design—rather than just in effect—regulatory structures.

In the Howard government's early years of office, the COAG-centred process went somewhat into recess, perhaps because it was too associated with the final years of the Keating Labor period and with an acceptance of the States as collaborative participants. It was largely on this basis that Galligan and Wright (2002) observed that 'the Howard Liberal coalition elected in 1996 has been unconcerned with federalism, showing little interest in, and giving no leadership to, COAG'. This is now clearly a dated observation. The COAG process has become very active over the past 5 years or so, addressing a number of crucial national issues—including counter-terrorism measures, a national water trading and water management system, and a national energy regulation system—for which significant progress depends on collaborative Commonwealth–State action.

The COAG negotiations confirm the States to be active participants in the intergovernmental system: as Keating and Wanna (2000, 138) observe, the COAG process implies that 'the Commonwealth ha[s] to accept the states' involvement in the determination of priorities and policy'. Characteristically, the key COAG outcomes have reflected not simply the Commonwealth's initial position but also the influence that the States have been able to bring to the negotiations. For example, it was at the insistence of the State Premiers that agreed complementary counter-terrorism legislation was modified to strengthen judicial review provisions and to regulate the use of lethal force by police undertaking preventive detention action. The referral of State powers to the new national regulatory bodies for water and energy—respectively, the National Water Commission and the Australian Energy Regulator—has been delayed while States manoeuvre and negotiate about details and timing. (In the case of water, this delay probably helped to provoke the Howard government's

¹²For an erudite State perspective on how the national interest seems easy to confuse in Canberra with the Commonwealth interest, see Bannon (1987).

later proposal for a full referral to the Commonwealth by the states of their powers over the Murray–Darling system.)

Equally characteristically, however, the eventual outcomes will, in effect, cede long-exercised State powers. By agreeing to collaborative national regimes subject to new structures of cross-governmental supervision and compliance, the States are ceding (vertically to a higher level in the federal system) some of their own capacity for autonomous action.¹³ By virtue of this process coinciding with a parallel shift in fashion about what is the appropriate role for government in general, the States have also weakened their capability by acceding to arrangements that promote or impose market-type structures and competition. Notable instances of this under the Howard government include the National Water Initiative (DPMC 2006) and the Market-Based Instruments Pilot Program within the National Action Plan for Salinity and Water Quality (DAFF and DEH 2006a).

The February and July 2006 COAG meetings instituted a new National Reform Agenda to replace the expiring NCP agreement. The Bracks Labor government in Victoria was the impetus behind the National Reform Agenda (Victorian Premier 2005) but it won eager Commonwealth support and has been endorsed in principle via COAG by all governments.

The National Reform Agenda has three broad components, labelled as human capital, competition and regulatory reform (COAG 2006). The communiqué describes the ‘competition’ component as ‘a substantial addition to, and continuation of, the highly successful National Competition Policy Reforms’. It aims at ‘further reform and initiatives in the areas of transport, energy, infrastructure regulation and planning, and climate change technological innovation and adaptation’—all likely to overlap with areas of State-level policy jurisdiction. The ‘human capital’ component is aimed squarely at the States’ core human services responsibilities for health and education. The ‘regulatory reform’ component seeks to ‘reduce the regulatory burden’ on the business sector ‘imposed by all three levels of government’ and in ‘six priority cross-jurisdictional “hot spot” areas’, including occupational health and safety, development assessment and building regulations. A new COAG Reform Council, replacing the National Competition Council, will oversee the implementation of the National Reform Agenda.

Pointedly, the Commonwealth successfully deflected State demands for a continuation under the National Reform Agenda of NCP-style compensation payments. Rather, such payments will be made on ‘a case-by-case basis’ on the basis of ‘the relative costs and proportional financial benefits to the Commonwealth, the States, Territories and local government of specific reform proposals’ (COAG 2006). Thus, the States have signed on to a continuation of an NCP type of process without the NCP’s inbuilt guarantees about financial benefit.

¹³As stated in the *Australian Nation Principle* agreed to by the Premier and Chief Ministers (in the absence of the Commonwealth) in November 1991, ‘All governments in Australia recognise the social, political and economic imperatives of nationhood and will work cooperatively to ensure that national issues are resolved in the interests of Australia as a whole’. Intended to counterbalance this was the *Subsidiarity Principle*: ‘Responsibilities for the regulation and for allocation of public goods and services should be devolved to the maximum extent possible consistent with the national interest so that government is accessible and accountable to those affected by its decisions’ (Premiers and Chief Ministers 1991).

Program Federalism: Tightening the Ties

Commonwealth conditional grants to the States, under the authority of Section 96 of the Constitution, have always had potentially important policy and program ramifications. Through these conditional grants, the Commonwealth has a backdoor mechanism for policy and program intervention in areas that are otherwise under State jurisdiction. The increasing proportion of Commonwealth funding that has been tied to specified conditions is a feature of the past half century. The shift was most pronounced during the tenure of the Whitlam Labor government of 1972–75, but all Commonwealth governments on both sides of the party divide have presided over this phenomenon.

There has been some academic controversy—or at least some inconsistent inferences and observations—over the actual policy significance of the conditions embedded in conditional grants. Some legal and economic analysts have followed the constitutional and financial trail to argue that the conditional grants system must significantly erode State-level autonomy in relation to the Commonwealth (e.g. Else-Mitchell 1983; Mathews 1983; Walsh 1989; Zines 1989; James 1992; Schapper 1993). A political science contingent has been more cautious, submitting that the States retain a significant political strength that seems to have the effect of protecting a great deal of their policy and program autonomy (e.g. Galligan 1988; Chapman 1990; Sharman 1990; Parkin and Summers 1996; Parkin 2007a). The States retain the jurisdiction to make the laws and directly deliver the services over a wide range of matters. Yet, however much politicians or officials at the Commonwealth level may wish to influence matters pertaining to, for example, hospital management or forest protection or numeracy programs or public housing tenancy management or prison custodial practices or servicing non-metropolitan regional centres, such everyday program management occurs largely within the State public sectors.

The limited empirical research suggests that the relationship between tied funding and the locus of policy control has varied between policy areas and over time (Galligan, Hughes and Walsh 1991; Parkin 1992; Clarke 1997). Even when the conditions attached to tied grants have been detailed and restrictive, this might simply reflect the consensual outcome of genuine intergovernmental negotiation in which the States, occupying the prime jurisdictional turf, can negotiate from a position of reasonable strength even if they desperately need the Commonwealth funds. Or it may reflect judgements from the States that they have little interest in the policy area—as, for example, with university funding. With some intergovernmental funding arrangements, the designated conditions attached to the Commonwealth grant have been quite general, leaving the States with wide discretion about how the funds are spent or permitting bilateral intergovernmental agreements endorsing how any particular State wishes to expend the funds in broad conformity with their intended purpose. This has meant that, in practice, Commonwealth involvement in areas of State jurisdiction has, in the past, typically involved a large measure of negotiation with and concessions to State-level actors.

Commonwealth–State interaction over hospitals and health services during the Howard period conforms to this historical pattern. The health domain is of major political and financial significance for both levels of government, and there is widespread recognition that the current cross-governmental arrangements can be problematic (Duckett 1999; Hancock 2002). Various proposals for clarifying and rationalising the respective roles of the Commonwealth and the States have been

promulgated over the years. Tony Abbott, as Commonwealth Minister for Health, has publicly contemplated a total Commonwealth takeover of the public hospital sector (e.g. Saunders and Schubert 2004; Stafford 2005). A Commonwealth task force headed by Andrew Podger, former Public Service Commissioner and head of the Department of Health and Ageing, has lent some support to this vision (Grattan 2005; see also Podger 2006a; 2006b). But both sides have so far veered away from any radical or even modest restructuring. Prime Minister Howard has signalled that the Commonwealth does not wish to assume responsibility for the troubled service-delivery end of the health system. Instead, ‘incremental change’ towards ‘finding practical options to improve the delivery of health services’ is the goal (Howard 2005).

More ubiquitously, across a raft of policy and program areas, there is evidence that, via a dogged insistence that it legitimately represents some sort of ‘national interest’ perspective and via some interesting managerial adroitness, the Howard government may be doing better than any previous Commonwealth administration in more tightly binding the States via conditional grants.

Further research work is under way on this matter.¹⁴ The evidence, by its nature, is hidden within the complex interstices of contract negotiations, administrative oversight procedures, matching grant formulae, other financial ‘input controls’, intergovernmental reporting protocols, periodic financial acquittals, accounting barriers intended to deter cost-shifting, bilateral State–Commonwealth discussions and sub-agreements, individual subproject approvals, and agency-to-agency and officer-to-officer cross-governmental interactions. The initial evidence suggests a concerted effort from Canberra, starting quite early in the Howard regime, to tighten up on program compliance, to insist on more serious State contributions via matching funds, and to insist on specific attribution of credit to the Commonwealth for program outcomes.

Countervailing proposals to loosen some of these controls have been blocked at the Canberra end. In March 1999, a States and Territories proposition for the Commonwealth to be satisfied with rigorously audited program outcomes rather than being obsessed with input controls was submitted to the Commonwealth Treasury, which was evidently sympathetic to the economic and managerial efficiency embodied in an output orientation. The idea subsequently emerged as an agreed Commonwealth–State Heads of Treasuries paper on *Principles for Specific Purpose Payment Agreements* (Heads of Treasuries 1999; see also ACT Government 2001; Allen Consulting Group 2006, 11). It was emphatically vetoed elsewhere in Canberra policy apparatus, reportedly via the Department of Prime Minister and Cabinet.

There is a growing list of areas in which Commonwealth Ministers have unapologetically been adamant that Commonwealth grant contributions are a vehicle for pursuing Commonwealth policy and program priorities. The education portfolio has been replete with examples, especially during Brendan Nelson’s tenure as Minister

¹⁴This research is under way via two projects funded by the Australian Research Council. Discovery Project DP06766174 (chief investigator: A. Parkin) is entitled *Regulatory Federalism and Public Policy: The Transformation of Australian Intergovernmental Relations*; this article is one of its initial products. Linkage Project LP0669283 (chief investigators: G. Craven, A. Fenna and A. Parkin) is entitled *Cooperation, Competition or Control? Public Policy and the Use of Tied Grants in Australian Federalism*.

of Education and his successor Julie Bishop looks like continuing in a similar, if less aggressive, vein. Some of the Commonwealth's education initiatives have been mostly symbolic, such as the June 2004 announcement that all primary and secondary schools would need to possess a functioning flagpole as a condition of receiving Commonwealth funding (DEST 2006a). Others have been highly interventionist, such as the requirements for public schools; that is, schools created by and owned by State governments—to specify performance targets and performance measures, to ensure that student reports are plain-English in composition and reveal where a student ranks in his/her class, and to publish school performance information (DEST 2005). The adoption of effective nation-wide curriculum standards is again on the agenda, framed from the Commonwealth perspective as a critique of the inadequacies of State-level educational governance (e.g. Ferrari 2006), notwithstanding manifest intergovernmental progress over recent decades in agreeing to national schooling goals and collaborative curriculum frameworks (e.g. MCEETYA 2006; Curriculum Corporation 2006).

Particularly controversial have been Commonwealth-imposed grant conditions unrelated to the immediate policy or program at hand, especially conditions promoting the Howard government's preferred position on industrial relations. The so-called National Construction Code insists that State government agencies must not accept tenders and/or expressions of interest from contractors for Commonwealth-funded projects unless they are code-compliant; that is, unless they 'facilitate greater flexibility and productivity' in workplace relations (DEWR 2006). While, notably, the Bracks Labor government in Victoria declined to accept a Commonwealth contribution to the costs of MCG reconstruction for the Commonwealth Games owing to the attendant industrial relations conditions, mostly the States have been prepared to accede to them.

Parallel Federalism: Commonwealth Unilateralism

A piquant Whitlamesque touch with respect to Commonwealth–State relations has probably been most striking in the Howard government's willingness to bypass the States, or compete directly with them, in pursuit of what it regards as national goals. Some examples among many include:

- The Roads to Recovery program, which commenced in February 2001 (and was later extended and subsumed within the broader AusLink program), aims to channel several billion dollars directly to local governments, notwithstanding that they are constitutionally creatures of the States (DTRS 2006).
- The Investing in Our Schools Programs Grants funds projects identified by 'school communities' that maintain and upgrade school facilities. Grants are made to organisations that the Commonwealth government recognises as 'Government School Community Organisations' or 'School Parent Bodies', in what seems to be a process that quite transparently refuses to acknowledge that public schools are creatures of State governments (DEST 2006b).
- Under the Australian Government Envirofund, part of the National Heritage Trust set up in 1997 with part-proceeds from the sale of Telstra, community groups and individuals can apply for grants that target local environmental issues (DAFF and DEH 2006b). Community Water Grants are designed 'to encourage wise water use' (DAFF and DEH 2006c).

- The National Community Crime Prevention Program provides funding for 'grass roots projects designed to enhance community safety and crime prevention' (Attorney-General's Department 2006).
- The establishment of Australian Technical Colleges was announced during the 2004 election campaign. The Colleges are intended to be specialist senior secondary schools in which students combine academic courses and trade training, in fairly explicit competition with the State-administered TAFE systems. Twenty-five colleges are envisaged; five had become operational by late 2006 and many others are due to open in 2007 (DEST 2006c).
- The Carrick Institute, which commenced operations in 2006, was created to 'promote and support strategic change in higher education institutions', mainly universities, 'for the enhancement of learning and teaching, including curriculum development and assessment' (Carrick Institute 2006). Nearly all Australian universities are legislative creatures of the States, yet the significance of Commonwealth financial contributions, conditional upon university compliance in relation to matters as detailed as course profiles and student service fees, means that even staunch federalists tend to concede the Commonwealth's de facto dominance (e.g. Craven 2006a; see also Craven 2006b; Norton 2005).
- Comcare describes itself as 'responsible for workplace safety, rehabilitation and compensation in the Commonwealth jurisdiction' (Comcare 2006). Under its Act, it can now cover companies 'deemed to be carrying on business in competition with a Commonwealth authority or with another corporation that was previously a Commonwealth authority' (Andrews 2006). Such companies are, in effect, invited to opt out of State-run schemes and instead to self-insure with Comcare. Recent examples of companies opting to do this include Optus, Linfox and K&S Freighters. The Commonwealth Minister for Employment and Workplace Relations has noted that 'the States have previously objected to companies seeking to leave their schemes and self-insure through Comcare. Therefore the onus is clearly on them to work together with the Australian Government. . .to put in place consistent and uniform self insurance arrangements across their schemes' (Andrews 2006).

Perhaps the most significant example of all is the Commonwealth's controversial 2005 industrial relations legislation (Roth 2005). Prior to its passage, Prime Minister Howard described the coincidence of opportunity, philosophy, politics and federalism in the following way:

[W]ith the favourable outcome in the Senate, we are now in a position to drive the industrial relations reform process further in ways consistent with liberal philosophy.

A single set of national laws on industrial relations is an idea whose time has come . . . [T]his is not about empowering Canberra. It is about liberating workplaces from Colac to Cooktown . . .

The current system of overlapping federal and state awards is too complex, costly and inefficient . . .

Our preference is for a single system to be agreed between the Commonwealth and the States. . .But, in the absence of referrals from the States, the [Commonwealth]

Government will do what it reasonably can to move towards a more streamlined, unified and efficient system. (Howard 2005)

On this issue the States determined to make a legal stand, challenging the Act on constitutional grounds in the High Court. By a 5-2 majority, the Court ruled for the Commonwealth in November 2006.

Not all attempts to bypass or annul State jurisdictional actions have been successful, as the experience of Senator Ian Campbell, appointed as the Howard government's Minister for the Environment and Heritage in July 2004, reveals. Campbell intervened controversially to counter several Victorian conservation initiatives, but with problematic results from a Commonwealth perspective.

Campbell's declaration in June 2005 of an 'emergency heritage listing' for alpine cattle grazing, in defiance of a Victorian determination to remove cattle from alpine areas, seems never to have carried any particular legal force, and by October 2005 the Minister had reportedly 'admitted defeat' (Fyfe 2005).

In April 2006, Campbell drew on his powers under the Commonwealth's Environment Protection and Biodiversity Conservation Act to veto a wind farm proposal that had been approved, after an environmental impact assessment, by the Victorian Minister of Planning. Campbell's claimed grounds for his veto were the possible impact of the wind farm on an endangered parrot species. His intervention was initially effective in bringing the development to a halt, amid considerable public controversy (including allegations that the decision, apparently popular in the local marginal seat of McMillan, had been politically rather than scientifically based). Victorian Premier Steve Bracks appealed directly to the Prime Minister to overturn Campbell's decision which, he argued, 'will introduce a great deal more uncertainty for investors' (Minchin 2006a). Getting no satisfaction from that option, the Victorian government, along with the developer, proceeded to launch a Federal Court legal challenge. By August 2006, Campbell had backed down, agreeing to reconsider his decision in return for a cessation of the Federal Court action (Minchin 2006b).

Federalism and Conservative Nationalism

The High Court's upholding of the Howard government's Workplace Relations Act, in the face of a constitutional challenge by five State governments, has been greeted with alarm by the State Premiers (Shaw and Ker 2006). The Court majority's determination in this *NSW v. Commonwealth of Australia* case, essentially finding that the Commonwealth's constitutional power over 'corporations' extends to a capacity to regulate industrial relations matters, amply confirms—and arguably extends—the legal predominance of the Commonwealth within the federal system.

It is important to note, however, that up until this significant decision the growing prominence of the Commonwealth during the Howard years had not been based on any significant legal claims or developments. The Howard government had mostly not attempted to take advantage of High Court decisions that hurt the States; for example, the Commonwealth-led rescue package of 1997 after the Court decisions disallowing various so-called excise taxes seems genuinely to have been constructed to restore the *status quo ante* as far as possible (James 1997). The Prime Minister has attempted to interpret the Workplace Relations decision within the same non-alarmist framework, although his invocation of a kind of 'national interest' wildcard has come to be quite characteristic:

We will not interpret this decision as being any kind of constitutional green light to legislate to the hilt. We have no desire to extend Commonwealth power, except in the national interest. I have no desire for takeover's sake to take over the role of the [S]tates. (Howard 2006)

Notwithstanding the outcome of *NSW v. Commonwealth of Australia*, the emboldened Commonwealth initiatives under the Howard government have mostly had a political and policy, rather than a legal, character. They seem to emerge from a maturing perspective that regards the Commonwealth government as the guardian of the national interest and the States as sectional interests whose actions may potentially harm the national interest.

Minister Tony Abbott had rehearsed an argument along these lines earliest and most adventurously:

[I]t's important not to be sentimental about the [S]tates. Accident as much as design has made Australia a federation. . . The issue is not whether Canberra knows best but whether the Commonwealth should be apologetic about the powers it has and bashful about exercising them to the extent necessary to put its policies into practice . . . This is not an argument to slash the [S]tates' formal constitutional powers, let alone abolish [S]tate governments. It's an argument for the Commonwealth to exercise robustly the powers that it has. (Abbott 2003; see also Abbott 2005)

In a speech to the Menzies Research Centre in April 2005, Prime Minister Howard put similar ruminations into his own personal, historical and philosophical framework. His nationalist inclinations were quite unmistakeable:

[T]he federal structure of our nation will remain . . . If we had our time again, we might have organised ourselves differently, but that is pure theorising . . . There has been some commentary of late that my Government has discarded its political inheritance in a rush towards centralism . . . These fears of a new centralism rest on a complete misunderstanding of the Government's thinking and reform direction. Where we seek a change in the Federal–State balance, our goal is to expand individual choice, freedom and opportunity, not to expand the reach of the central government . . . The goal is to free the individual, not to trample on the States. We have no desire to take over functions that are being properly discharged by States and Territories. On the contrary, with the GST, my Government delivered the most important federalist breakthrough since the Commonwealth took over income taxing powers during World War II . . . I am, first and last, an Australian nationalist . . . I have little time for State parochialism . . . [O]ur first impulse is to seek cooperation with States and Territories on national challenges where there is overlapping responsibility. But I have never been one to genuflect uncritically at the altar of States' rights. (Howard 2005; see also Kelly 2006)

The long-term impact of this conservative nationalism might be quite substantial. It could prove to be the most enduring legacy of the Howard governments. Then NSW Premier Bob Carr was reported in March 2005 as claiming that 'John Howard and Costello are turning the [S]tates into implementation agencies of a very powerful [C]ommonwealth' (Clark 2005). Tony Abbott in July 2006 anticipated 'the withering away of the [S]tates . . . [to become] less like sovereign governments and more like branch offices of Canberra' (Lewis and Price 2006), and a week later Peter

Costello likewise envisaged the States as 'moving towards the role of service delivery more on the model of divisional offices than sovereign independent governments' (Costello 2006a). The explicit references to the notion of sovereignty, surely fundamental to the basic definition of an authentic federal system (Parkin 1996a, 4–7), are telling.

However, there are also good reasons for political scientists to continue to be wary of yet another set of predictions about the inexorable decline of the States, especially in view of the States' unaccustomed (relative) financial comfort in the post-GST environment. The States have managed to deny a succession of such predictions throughout the twentieth century, and in some ways they emerged stronger at the century's end than they had appeared in its middle years. The COAG process, notwithstanding its effect of shifting key State powers to collaboratively endorsed national bodies and protocols, continues to legitimise the States, and especially their leaders, as key political actors. The States have also undertaken some interesting, although as yet tentative, moves to institute collaborative intergovernmental arrangements that bypass the Commonwealth. A cross-State national carbon trading scheme has been proposed, and a new State-constituted Council for the Australian Federation—envisaged as a COAG without the Commonwealth—met in October 2006.

John Howard has notably *not* supported the more adventurous of his Ministers when they advocate wholesale Commonwealth takeovers of key State service areas such as public schools (e.g. Wroe 2005), public hospitals (e.g. Kenny 2006) or mental health (e.g. Hodge 2005). Likewise, Treasurer Costello is on record as advocating the withdrawal of any direct Commonwealth interest in health and education as a trade-off for the Commonwealth acquiring 'full accountability and powers in relation to the national economy' (Shanahan 2006). 'The states will always run the schools', he later pronounced. 'The [C]ommonwealth doesn't employ the teachers and I can't imagine a situation where it would' (Costello 2006b).

Although Australian federalism will emerge from the Howard period transformed in important ways, it is likely to continue to be the dynamic, robust and enduring phenomenon to which we have become accustomed. Notwithstanding perturbations and partisan grandstanding from time to time, this will continue to make intergovernmental collaboration rather than wholesale confrontation a sensible strategy.

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