



COMMONWEALTH OF AUSTRALIA

Official Committee Hansard

SENATE

SELECT COMMITTEE ON THE REFORM OF THE AUSTRALIAN
FEDERATION

Reform of the Australian Federation

THURSDAY, 5 MAY 2011

CANBERRA

BY AUTHORITY OF THE SENATE

INTERNET

Hansard transcripts of public hearings are made available on the internet when authorised by the committee.

The internet address is:

<http://www.aph.gov.au/hansard>

To search the parliamentary database, go to:

<http://parlinfo.aph.gov.au>

ORIGINATING CHAMBER

JOB NAME

JobDate

Senators in attendance: Senators Back, Moore, Ryan and Trood

Terms of reference for the inquiry:

To inquire into and report on:

(a) key issues and priorities for the reform of relations between the three levels of government within the Australian federation; and

(b) explore a possible agenda for national reform and to consider ways it can best be implemented in relation to, but not exclusively, the following matters:

(i) the distribution of constitutional powers and responsibilities between the Commonwealth and the states (including territories),

(ii) financial relations between federal, state and local governments,

(iii) possible constitutional amendment, including the recognition of local government,

(iv) processes, including the Council of Australian Governments, and the referral of powers and procedures for enhancing cooperation between the various levels of Australian government, and

(v) strategies for strengthening Australia's regions and the delivery of services through regional development committees and regional grant programs.

BERESFORD-WYLIE, Mr Adrian, Chief Executive Officer, Australian Local Government Association	1
DOHERTY, Mr Dermot, Assistant Secretary, Commonwealth Grants Commission	12
ENGLISH, Mr Dominic, First Assistant Secretary, Department of the Prime Minister and Cabinet	37
FITZPATRICK, Ms Mandy, Manager, Commonwealth State Relations Division, The Treasury	37
GALLIGAN, Professor Brian, Private capacity	22
PERRY, Mr Ronald Thompson, Assistant Secretary, COAG Unit, Department of the Prime Minister and Cabinet	37
SPASOJEVIC, Mr Janko, Secretary, Commonwealth Grants Commission.....	12
UHR, Professor John, Private capacity.....	30
VROOMBOUT, Ms Sue, General Manager, Commonwealth State Relations Division, The Treasury	37

BERESFORD-WYLIE, Mr Adrian, Chief Executive Officer, Australian Local Government Association**Committee met at 11:16**

CHAIR (Senator Trood): I declare open this public hearing of the Select Committee on the Reform of the Australian Federation, the fourth in a series of public hearings the committee is holding in relation to its inquiry. The committee is to report by 20 June 2011. I welcome you all here today and I remind everyone that the witnesses giving evidence to the committee are protected by parliamentary privilege. Any act which may disadvantage a witness on account of their evidence is a breach of privilege and may be treated by the parliament as a contempt. It is also a contempt to give false or misleading evidence to a committee. Witnesses should be aware that if, in giving their evidence, they make adverse comment about another individual or organisation, that individual or organisation will be made aware of the comment and given a reasonable opportunity to respond to the committee. The committee prefers to hear evidence in public but we may agree to take evidence confidentially. The committee may still publish confidential evidence at a later date, but we would consult with witnesses concerned before doing this.

Our first witness is Mr Adrian Beresford-Wylie of the Australian Local Government Association. Welcome, Mr Beresford-Wylie. We have received a submission from your organisation which we have labelled submission 24. Do you wish to make any amendments to that submission at this stage?

Mr Beresford-Wylie: No, Senator.

CHAIR: We will be very happy to have an opening statement from you, if you care to make one, and then we will ask you some questions.

Mr Beresford-Wylie: Thank you for giving me the time, Senators, to appear before you this morning. I do not wish to make an extensive opening statement. You have our submission, which has attempted to deal with the issues that you have before you in your terms of reference. In particular, of course, there is material in there relating to the position of the Australian Local Government Association with regard to the constitutional recognition of local government.

We have also provided some commentary on the Council of Australian Government's processes. The Australian Local Government Association's president is a member of COAG and a member of 13 other ministerial councils—that is to say, the ministerial councils that exist until 30 June, and then there is reform. Local government expects to and I think will play a role in the councils that will exist after 30 June.

We have also provided a little bit of commentary on regional development and what we see as local government's important role in that area. I am happy to answer any questions the committee might have.

CHAIR: Thank you very much. Before I start the questions can I say that I think your submission provides the committee with a pretty clear understanding of the kinds of challenges that local government across the country confronts at various levels, particularly in relation to revenue activities. I personally am very grateful for that and it will be very helpful to the inquiry. I am sure my colleagues will take up the question of constitutional recognition of local government, but I might begin with the point you make about the challenges in relation to local government raising revenue. You make the point about rates being the major source of revenue. Given the challenges that local government face, in the absence of a possibility that there may be increasing Commonwealth funds, or indeed state funding, do you see any other alternatives for local government raising the kind of revenue it needs to perform its expanding services?

Mr Beresford-Wylie: We have two major sources of revenue that appear in an analysis of local government revenue. The first one is rates. We collect about three per cent of Australia's taxation revenue. Property rates are running at about \$10 billion. Our second major source of revenue are fees and charges. I think rates are about 40 per cent of our revenue. Fees and charges amount to more than 30 per cent. That figure is proving a little escalated by the fact that in Queensland, western New South Wales and Tasmania local government provides water and sewerage. Therefore, that fees and charges figure includes what would otherwise be considered to be state revenue or revenue of privatised entities in other jurisdictions, so it is slightly higher. Rates do remain our major source of revenue.

The Productivity Commission carried out an analysis of local government's own-source revenue raising capacity a few years ago, and it made a couple of observations. One of them was that local government was probably raising about 90 per cent of its hypothetical revenue raising effort which, from my perspective, I would suggest is a good effort for a level of government. Local government is a democratically elected level of government. Yes, it delivers services to local communities, but we do in fact have more than 6,000 councils who

are represented, and therefore represent their constituencies at local, level. That means we are responsive to the community and to its pressures, and we have to recognise that in setting rates one of the things we have to consider is the capacity of individuals to pay those rates, the capacity of the community to a better rate increases. Councils are very sensitive about how they deal with that issue.

Since we are at a level which is about 90 per cent revenue raising capacity that is a very high level. I suspect, if one considers the tax base of other levels of government, it might be a little higher. I think that constrains our ability to raise revenue through those rates. There are a large number of councils, particularly in regional areas, which have very small rates bases. They would certainly be constrained about their ability to raise rates, and there are of course some state constraints on local government's ability to raise revenue. There is rate capping in New South Wales and in the Northern Territory.

So in terms of local governments ability to raise revenue, we face a difficulty. We did commission some work from PricewaterhouseCoopers in 2006 and they actually presented some recommendations about how local government might address its financial sustainability. They estimated that between 10 and 30 per cent of councils would face financial sustainability problems unless they tackled the issue. They made a series of recommendations about how we might go about approaching other levels of government for an increase in revenue and they made some recommendations about how local government itself might look at sharing services and improving its asset management to try to deal with some of the revenue challenges we face, coming at it from the opposite direction. I think it is clear that, in the absence of revenue reform, local government simply has to look at the sorts of services and infrastructure it provides to make sure that it can live within its constraints. That may mean that some of those standards of service and the levels of service are going to be constrained in the future.

CHAIR: You make the point that the expectations that are being placed upon local government have been increasing over the last decade, and perhaps even longer, which are putting increasing demands on the revenue that local government is able to generate, but not necessarily has there been a significant increase in its sources of revenue. Your submission refers to the Regional and Local Committee Infrastructure Program, which is about a billion dollars. To what extent will that alleviate the problem?

Mr Beresford-Wylie: I think that will go some way towards alleviating the issue for local government. But I must say that one of the recommendations of PricewaterhouseCoopers was to try to address that backlog in renewals for community infrastructure. We were quite disciplined in putting a position to the government of the day, which was the previous government, and this current government in saying that we were looking for assistance in the area of community infrastructure but we were cautious about a program that would actually lead to the construction of new infrastructure. We had hoped that the focus would in fact be on addressing our existing infrastructure and the backlog. So rather than building a new problem, we would address the existing problem.

The program that was put in place was a generous program. It did provide funding to councils to address community infrastructure issues; although, obviously some of the infrastructure that was provided was new infrastructure that was constructed over the two-year period. Of course the program was also designed to address the issue of the local impacts of the global financial crisis and to provide a stimulus to local economies. I dare say that it has been a very successful program, particularly that portion of the program that has flowed directly to councils where many thousands of projects have been completed at a local level. We are talking about \$450 million of the \$1.1 billion of funding that has gone directly to councils on an allocation basis. I think it has had a very positive response from councils and from local communities, and the government seems very pleased with the outcome. I think it has made a difference to the infrastructure backlog but not the same level of difference that would have been made had we had a program that concentrated specifically on existing infrastructure backlogs.

CHAIR: This is not a continuing program is it? It was a two-year program.

Mr Beresford-Wylie: No, it is a program that is terminated now. There is a program that has been announced under the Regional Development Australia fund, which is aimed also at the issue of community infrastructure but not specifically restricted, however, to local government. Non-government organisations—incorporated non-government bodies—are able to apply as well; they are eligible applicants under the program. The first tranche of that program, \$100 million, is currently open for councils to apply for. It is an applications based program not an allocations based program. I think applications close on 13 May.

CHAIR: But your case here is that there are special needs for local government which are not being met through other means of revenue and that those demands on local government are increasing.

Mr Beresford-Wylie: That is correct.

CHAIR: For which it may be some of advantage to you to have access to another pot of money. But if you are competing with other levels of government then it is not serving your particular needs, is it?

Mr Beresford-Wylie: That is true. The issue was drawn out at a national level by PricewaterhouseCoopers. Drawing on a series of reports that have been produced at the state level, they identified the fact that a number of councils were facing pressure, particularly in delivering ongoing services that their community wanted. Councils were being faced with the challenge of doing a range of services that they had not done in previous decades. These were human related services.

In order to deal with the current service demands, councils were tending to reduce their level of depreciation and investment in renewals for the infrastructure. That is a growing problem. Councils are meeting the day-to-day obligations and the increased service demands of their communities. They are very responsive to those demands but it was showing up in the area of that infrastructure renewal. That is an issue which remains to be addressed. The most recent assessment we have of the likely backlog and gap in road funding for local government, a report we produced and released at the end of last year, suggests the annual gap over the next 20 years is probably about \$1.2 billion—that is the gap between what we need to spend to maintain the standards of service for local roads and what we have access to in revenue.

CHAIR: Does that take account of the impact of floods in various states?

Mr Beresford-Wylie: No, this was an ongoing thing rather than taking account of the immediate impact, which has emerged during the summer period. It was before that.

CHAIR: I will give my colleagues an opportunity for questions and will come back to you.

Senator MOORE: Thank you for your submission. As you well know, because your organisation has been following the evidence that we have received, there has been quite a degree of discussion about the recognition of local government in the Constitution. Your own submission looks at the role of the Local Government Association up till now and I know that will be ongoing. But in your last paragraph you say:

... it is subject to considerable uncertainties because it has no formal place in the nation's Constitution.

Would like to expand on that? Why do you say that the role of local government and the existence of local government is uncertain because of the lack of recognition in the Constitution?

Mr Beresford-Wylie: In terms of our capacity to be ongoing as a financially sustainable level of government I think we face a significant challenge simply because of the nature—and I am going to be blunt here—of the vertical fiscal imbalance that exists in our federation. The Australian government, of course, has accrued taxation powers and collects a sizeable proportion of the taxation—probably around 83 per cent. Local government has a very small taxation base. It has a growing demand in terms of the services and infrastructure its communities expect, and I think reasonably expect. It has a very strong relationship with, and indeed, as people would say, is a creature of, the states, who find themselves under a lot of pressure in terms of the sorts of services they provide. They provide the big, expensive services in terms of public transport, health and education, and they face revenue constraints as well.

Local governments' lack of recognition in the Constitution and the uncertainty that exists around the ability of the Commonwealth to invest directly in local communities pose a challenge for local government in the future. One of the things that we have been keen to tread around very cautiously is the nature of any recognition we might seek through the Constitution. There has been a lot of discussion and debate over 30 years on the nature of that recognition, and after an extended process taking more than three years ALGA has come down on the side of a very simple and pragmatic change to the Constitution to address what we see as an ongoing issue, which is not intended to impinge upon the nature of the relationship with our state governments and the accountability framework under which we live.

Senator MOORE: So it is a minimalist approach?

Mr Beresford-Wylie: It is, but it is a reflection of the fact that our research tells us a couple of things about what people will deal with in terms of constitutional recognition. They are not interested in symbolic changes to the Constitution. They are interested in changes that actually have an impact on themselves and in fact that either fix a problem or make life better at a local level for individuals. I will be blunt and say it did not emerge during our discussions with councils that they favoured some sort of broad reform which would see them move away from their current relationship with state governments. A lot of councils were certainly of the view that they had a tough time dealing with their state governments, but they thought that would be nothing compared to dealing, quite frankly, with the federal government if it had direct control over local government. So they shied away from any suggestion that there be a change in the Constitution to give the federal government control over local government.

Senator MOORE: But you also did not want to go into a clear definition of roles process?

Mr Beresford-Wylie: I think the difficulty there is an obvious one—that is, those changes that occurred at the state level, with the state government saying to local government in the last 15 years or so: 'We used to tightly prescribe the sorts of things that you did in legislation. We are happy to grant you general powers of competence—that is to say, you, local government, can provide services and infrastructure that your community wants as long as it is not illegal, as long as it does not conflict with state government policy and as long as you think you can afford it.' That is the challenge that local government has had. I think attempting to define those roles really is incredible in terms of a specific role definition.

Senator MOORE: I hope I am not going to intrude on your line of questioning, Scott.

Senator RYAN: I will probably pursue it after you.

Senator MOORE: One of the things we have talked about in the committee is the fact that the nature, the size, the activity and the competence of local government across the states varies enormously, so to make a standard argument for the variation of local governments is an issue in terms of people looking at any kind of change. I am from Queensland, as is Senator Trood, and we have gone through the process of amalgamations and have sizeable local governments now with significant budgets. So, from my perspective locally, it seems to be a reasonable request that that level is put in the Constitution. But in other states the whole role of local government is much different and their political history has been dynamic. I am interested in whether the association has a response to the fact that the constitutional change would be impacting on types of local government that vary enormously across our country—much more so than the types of state government. You can make an argument that the states vary enormously as well, and people have made that argument, but just the sheer number of local governments makes things more difficult.

Mr Beresford-Wylie: That is right. My observation would be that there are 560 or so local governments and they do vary enormously in their capacities; but, in a sense, local government is just that: it is local. It needs to be looked at in context. We have the local governments, which we need, to suit local conditions, all which state governments have determined will be the way that local government operates in their individual jurisdictions. Because of that, the change we are seeking really talks about the capacity of a federal government to directly fund local government. We are not talking about some sort of institutional recognition of local government, whatever that might be, or the preservation of local government bodies in their current form or whether their boundaries should be changing or not. That really is a matter for state governments. We operate under state legislation and state accountability frameworks. For that reason, we are quite comfortable with the idea that we have addressed a very narrow focus for that recognition, which is not intended to give local government and individual local government bodies a status that they do not currently have.

Senator RYAN: I want to explore this issue further. It is fair to say, is it not, that the outcome of the Pape case is not clear cut and certain? The outcome of the Pape case was not, with a majority judgment, that the Commonwealth cannot fund local government.

Mr Beresford-Wylie: We took some advice on that.

Senator RYAN: But there are conflicting judgments. The point I am making is that it is not certain one way or the other. I accept that there is doubt, because some judges wrote that there could be doubt, but it is not certain—there is no ruling—that the Commonwealth cannot directly fund local government as we stand today, is there?

Mr Beresford-Wylie: I would argue that it follows three other judgments, which essentially say that the Commonwealth's capacity to fund things not covered by section 51 is far more constrained than they thought it was.

Senator RYAN: Funding is still in place today, though, is it not?

Mr Beresford-Wylie: It is. If you are asking if they specifically ruled that funding under, for instance, Roads to Recovery was unconstitutional, I would have to say no.

Senator RYAN: I think it is an important point to make in this debate that there is some confusion about whether the Commonwealth has stopped funding local government, which it has not.

Mr Beresford-Wylie: No, it has not.

Senator RYAN: You say that you would like a power to directly fund—I think that is how you described it—not an institutional recognition. I do not mean to verbal you; I am paraphrasing what you said earlier. Is that a fair characterisation?

Mr Beresford-Wylie: It is.

Senator RYAN: Are you looking at a section 96 type arrangement? We have to recognition of the institution in order to be able to fund it, because you cannot fund something that is not at least vaguely described. The states are in the Constitution because they were the direct authorities delegated by Westminster under the colonial self-government act when we formed the Commonwealth of Australia. Are you looking at the recognition of local government in a section 96 type arrangement or a head of power to fund local government in a section 51 type arrangement?

Mr Beresford-Wylie: A section 96, not a section 51.

Senator RYAN: Would there be a description of local government somewhere else in the document?

Mr Beresford-Wylie: No, not necessarily.

Senator MOORE: Is that your position?

Mr Beresford-Wylie: That is correct. I should point out that this is a position that draws on the ALGA board's position.

Senator RYAN: I appreciate that.

Mr Beresford-Wylie: And it is a position that draws on the advice we have received.

Senator RYAN: You may have picked up that I am slightly more sceptical of this than Senator Moore is. I will get to this point, then. If we get a section 96 type arrangement, those grants can be tied, can they not? The Commonwealth does not usually hand over money. Historically, it has ratcheted down the amount of money it has handed over as financial assistance grants that are untied. A section 96 type arrangement would say that the Commonwealth can directly fund you on the basis of certain conditions.

Mr Beresford-Wylie: Yes. Parliament can appropriate the funds on whatever terms and conditions—

Senator RYAN: Therefore, the terms and conditions that the Commonwealth parliament can attach to those grants can be completely unrelated to the grants.

Mr Beresford-Wylie: It is entirely up to them and what parliament approves.

Senator RYAN: I am just looking at the behaviour of this parliament, which for over a century has been increasing the scope of its activities rather than maintaining them where the founding fathers intended. My concern here is that if there is a section 96 type of arrangement the Commonwealth parliament could continue to fund Roads to Recovery programs on the basis of planning laws that the local government may be forced to adopt, which may be in contravention of particular state policy wishes but the Commonwealth would then override the states by virtue of its power in section 109. Do you see what I am saying? There is the possibility of tied grants here that would allow the Commonwealth parliament to dramatically increase its scope and control over what local governments do.

Mr Beresford-Wylie: I must admit that it is not something that I had thought a Commonwealth parliament would try to do. I am not aware that it happens at the state level; I might be wrong. For a set of grants there is normally a set of terms and conditions that apply to those grants which relate specifically to what the funds are being appropriated for. If you are suggesting that there would be an attempt to tie grants to some outcome in some other area—

Senator RYAN: There is a long history of that. I know you may not have imagined that, but I imagine the people who wrote our Constitution did not imagine many of the things that the Commonwealth parliament does today as well. My concern here is that if a tied funding grant power is given to the Commonwealth parliament to directly fund local government on the same terms as it could fund the states, it dramatically opens the door for the Commonwealth parliament to start directing the activities of local government.

Mr Beresford-Wylie: I am not sure I can accept what you say. I can understand why you are putting that position, but I would suggest that there are a couple of things. First of all, I would hope that the Commonwealth parliament might recognise it. I can say from the history of the Australian government that I have not actually seen the Australian government necessarily intrude in a significant way into local government.

Senator RYAN: Not yet.

CHAIR: I think it is a kind of 'Be careful what you wish for' kind of question.

Senator RYAN: Call me devil's advocate.

Mr Beresford-Wylie: Yes, but I think for what you are suggesting I would have to be blunt. The Financial Assistance Grants are currently provided under a power whereby they are untied, but the Roads to Recovery grants are tied specifically to the outcome of roads. In a sense they are grants, I suppose. Realistically, if a Commonwealth government attempted to influence local government in a variety of different areas that were

inconsistent with state legislation and inconsistent with the practices of local government then there would be a very serious question about whether local government would accept those grants.

Senator RYAN: Historically, I think it was a former Labor prime minister who said, 'Never stand between a premier and a bucket of money.' If we add this power one might want to add 'local councillor' or 'mayor' because as you have outlined so comprehensively in your submission you are under substantial funding pressure. The history, as this parliament has aggregated taxing power to itself, has been that other levels of government—mainly state—in dire need of financial support as their taxing powers have been removed have ended up acquiescing to the demands of the Commonwealth parliament simply to get to the cash.

Mr Beresford-Wylie: I think we would still fall under the legislative control of the states.

Senator RYAN: What really concerns me is that the consequences of this have not been aired. For example, if there was a funding power under section 96 it would be very easy for the High Court to determine that a tied grant which the local government accepted may then allow the Commonwealth to set terms and conditions for that grant and the activities of local government in that sphere or in other spheres. This could then trigger the section 109 provisions which would mean that the Commonwealth legislation overrode that of the states. Therefore, any state laws that managed local government or required certain accountability measures that are inconsistent with the grant that the Commonwealth parliament had legislated and appropriated for may then be deemed void because the Commonwealth parliament clearly has superior legislative power within areas of its competence.

Mr Beresford-Wylie: I find it difficult to comment on something that is so hypothetical. While you say it may be easy for the High Court to reach that conclusion, I am afraid that I cannot share the view that the High Court is easily persuaded of anything.

Senator RYAN: I suppose my point is that when we deal with constitutional amendments we deal with hypotheticals because it is not something that can be undone. Similarly, I would venture to say that it is not an unrealistic scenario at all. It is less complex than the 1940s cases where the Commonwealth appropriated the states' taxation powers by adding one or two Commonwealth powers together. The unforeseen consequences of this might mean that your wish to still maintain your relationship with state government is in fact completely destroyed. It would then be up to the Commonwealth parliament to determine your relationship with the states.

Mr Beresford-Wylie: As I said, I can only work on the basis that the Commonwealth, as you point out, funds local government through Roads to Recovery. It has had the opportunity to influence that expenditure—which it has done—to determine that it be spent on roads. It has had the chance to move into other areas in terms of a relationship with local government and it has not really chosen to develop that relationship along the lines that you are suggesting. So I am really not in a position to comment. I know that you said it was a hypothetical, but I have some difficulty going that far along a hypothetical path.

Senator RYAN: With all due respect, I will give you another example that is ridiculously obscure. In 1995, when the Victorian and Western Australian parliaments passed a law that meant that students did not have to pay student union fees at universities, this parliament went to the trouble of passing another law that meant that whatever money the student unions lost by virtue of students of not joining was removed from the financial assistance grants—the untied grants—given by the Commonwealth parliament to the states and then handed to the student unions. I could give you 20 or 30 examples of behaviour like that where, quite frankly, a micro level of interference in the domain of state legislative responsibility has been undertaken by this parliament. I venture to say that as soon as you put yourself on a document you may find yourself in exactly the same situation. One author described it as 'a hundred years of tears' with respect to the autonomy of the states under the Commonwealth constitutional arrangements. So I do not think it is fair to say that it is particularly hypothetical. Do you have a response to that, given the experience of the states over a century?

Mr Beresford-Wylie: I do not have a response to that.

Senator RYAN: It is still possible, even if Pape held, that there could be no direct funding. Let us say that there was another case, Pape II, in a few years that said that the Commonwealth's appropriations power was limited to section 51, the other scattered direct powers and also section 60, which was considered under Pape. It is also entirely possible for the Commonwealth to give money to local government via the states via section 96 grants. For example, they could give all the Roads to Recovery money through section 96 tied grants to the states to then be passed on without a ticket being clipped by state parliaments or state governments. That is still entirely possible under the scenario of Pape being taken to its extreme conclusion.

Mr Beresford-Wylie: If you are asking me if the answer is yes, the Commonwealth can fund what it likes in terms of section 96 as long as it goes through the states—you are quite right.

Senator RYAN: So what is the problem with that? What is the problem with the Commonwealth parliament dealing with the six or eight organs—which, quite frankly, have a lot more capacity to deal with something as complex as the Commonwealth? For the city of Yarra—where I live—the city of Maribyrnong and all the ones scattered around Melbourne in country Victoria in my home state, the state government could get the money on condition that it is passed on in these amounts to these councils, so there is no ticket clipping and commission taken on the way. What is the problem with that arrangement?

Mr Beresford-Wylie: The only comment that I would make there is that the quantum or the base level of financial assistance grants has not changed since 1990. While the view that you are putting forward sounds reasonable, I have not seen any evidence that successive Commonwealth governments have been willing to increase the financial assistance grants that they provide to local government. They have chosen to go through a different mechanism, which is the provision of funding under Roads to Recovery and a variety of other programs rather than expanding those financial assistance grants. That is hardly surprising, given that their experience with the states is that while the states do pass those financial grants on, as you have said, without delay—and the states do not take a cut of those financial grants—in some instances historically the states have taken credit for that funding. There have been documents produced by state treasurers in particular, who have announced that their support for local government has been in the order of \$300 million or \$400 million. It is only when you drill down a little bit further that you discover that the majority of those funds are in fact financial assistance grants from federal governments. That is in indication of why Australian governments of all colours have not increased those financial assistance grants for many years.

Senator RYAN: I am a politician, so people may cynically accuse me—and I am not saying that you would—of being slightly craving of publicity. The ability to claim credit funding is surely not a rationale to change the Constitution.

Mr Beresford-Wylie: No. But the ability of local government to have a relationship with the Australian government that allows the Australian government to reach a partnership agreement, if you like, on what it is going to fund for councils and to deal directly with local communities seems to me to be a good reason to change the Constitution. It is about ensuring that local communities get the services that they need and deserve; it is not about some sort of grandiose idea that individual councillors will achieve some degree of recognition.

As for the idea that governments like to achieve an acknowledgement of their support for communities, frankly that is what our Roads to Recovery funding signs and a variety of other signs we have indicate—that when governments go through the pain of raising taxation they expect some degree of acknowledgement from communities that they are playing a role in the provision of services and infrastructure in those communities.

Senator RYAN: The capacity of some councils though to effectively work with the Commonwealth parliament differs. The untold story of COAG is that a number of our state and territory governments actually lack the capacity to deal with some of the complex issues that are undertaken at COAG because there is a critical mass issue here. When the Commonwealth department of whatever is responsible for local government at a given time is dealing with a council that might have 3,000 or 4,000 ratepayers what worries me is that even a small state has a lot more capacity to represent the interests of its people than does a small organisation like that up against the behemoth of the Commonwealth.

Mr Beresford-Wylie: I would make two comments there. The first one is that the Commonwealth is already doing that through Roads to Recovery. It is already dealing directly with those councils. The second thing is that the Commonwealth's ability to deal directly with those councils, even under a changed version of the Constitution, would really depend on what those councils could actually do. As we already established when we discussed it this morning, councils do not have an unending capacity to deal with the issues raised by their local communities. Some of them are very small. The things that councils have in common generally are to do with roads, bridges, community infrastructure and waste disposal. They are not into a variety of different areas. Those are the things that they actually do.

When we talk about a direct funding relationship between the Commonwealth and local government it would have to be on the basis that a council is able to actually play a part in a relationship that it has. For many councils that will be a constrained relationship. I am not suggesting that somehow councils will be able to do everything and that there would be a significant engagement with the federal government which would cause a significant problem for councils. Most councils—in fact, all councils—seem to be dealing effectively with the relationship they have currently with the federal government department under Roads to Recovery. I cannot see that there would be a difference if there was a different type of funding going to councils, as long as it was a type of funding that was addressing an issue which those councils were capable of dealing with—and that is going to be fairly narrow.

Senator RYAN: You have a more charitable view of what the Commonwealth parliament gets up to over time than I do.

Senator BACK: Mr Beresford-Wylie, in your submission you made reference to the fact that:

In each of the states and territories in the last 10-15 years, the relevant legislation creating and regulating local government has been reviewed and significantly amended, or replaced with new legislation ...

And you have made the observation that in many instances that was the first in 50 years. In those upgrades to the legislation with greater powers consistent with principles of general competence, in general terms, where have the relationships of funding between local governments and state governments been addressed?

Mr Beresford-Wylie: Those reviews have tended to be of those accountability frameworks and those powers.

Senator BACK: The opportunity must surely have been there, given the tension between state and local governments in terms of funding availability, to have addressed the funding question and the difficulties that local government faces?

Mr Beresford-Wylie: The opportunities may have been there but they have not been addressed.

Senator BACK: They have not been?

Mr Beresford-Wylie: No. One of the things that characterises local government and its relationship with state governments has been a tradition of cost shifting. We saw an examination of that issue by the Commonwealth Grants Commission at the beginning of this decade.

Senator BACK: I also note that you go further and say in terms of distribution there was a move away from property based services to human based services between the early 1960s and the late 1990s, and you make mention of recreation, culture, housing, community amenities, education, health, welfare and public safety services. Nearly all of those are actually state responsibilities under the Constitution. It seems to me that the argument being put is that local government is increasingly being asked to shoulder services that are constitutionally state services but without the funding following. Is that the case you are making?

Mr Beresford-Wylie: It is.

Senator BACK: And therefore why hasn't there been a greater effort at ALGA level to address this iniquity through the state constitutional process rather than an attempt to amend the federal Constitution?

Mr Beresford-Wylie: There have been efforts, but the efforts have been made at the state and local government association level rather than the Australian Local Government Association level. We exist to have an interaction at the national level. Some of those state local government associations will have appeared and no doubt will have spoken for themselves. They have a very active and ongoing relationship with their state governments, obviously, where they put the position on a constant basis that the relationship between the state governments and local governments should be one where adequate resourcing is provided to local governments for them to carry out the responsibilities that they have accrued, often under state legislation.

Senator BACK: Do you believe that the states and territories in general support the local government move to amend the Constitution to include local government in the Constitution?

Mr Beresford-Wylie: It is an interesting issue that is yet to be resolved. One of the things that we, the Australian Local Government Association, are doing is that we have a campaign to address this issue. One of the things that we have is a relationship with each of our member associations. Those member associations are raising the issue of constitutional recognition in terms of what we are putting forward, and I must say that these are only the terms the Australian Local Government Association is putting forward. The Australian government obviously has not said what it might do in terms of recognition.

Senator BACK: In relation to exactly that question, what role if any did your association have in the establishment of the 55 regional development authorities?

Mr Beresford-Wylie: The RDAs?

Senator BACK: Yes.

Mr Beresford-Wylie: We were consulted with by the government when it was in opposition. They discussed with us the nature of our relationship with the previous ACCs, area consultative committees, and what they might do or how they might move forward in regional development. One of the things we stressed to them was the idea that any move towards a regional development structure must not lose the benefits that accrued from being able to interact with local government. Local government is in place and has been in place in jurisdictions for more than a century. It has dealt with economic development issues. We did not want to see a situation where local

government was marginalised or where what was put in place was a duplicative set of administrative arrangements.

Senator BACK: I wonder if you could respond to a comment that was made by the Minister for Regional Australia, Regional Development and Local Government in October last year in which he said:

Entrenching local empowerment and regionalism in a whole of government approach at the Federal level will clearly have knock on consequences at the State and Local Government levels.

How do you interpret what he said?

Mr Beresford-Wylie: I would interpret that as saying that local government, state government and federal governments will be working together more effectively if they are trying to achieve some of the regional interests that they have. The announcement of RDAs took place after a discussion that had taken place within the Regional Development Council, a ministerial council that was established to look at regional development issues. There was quite a discussion about the proposition from the Australian government that it wanted to achieve a greater synergy between local government efforts for economic development, state government efforts and the federal government and to try to bring together a greater collaboration of effort so that the resources were directed towards shared goals. I would interpret it as being along those lines.

Senator BACK: I have a view that in our Federation it is critical that no one level of government has too much power. The concern that I have and that I put to you for your response is that a move of the type that you suggest would certainly give one level of government too much power. He who holds the gold makes the rules. Would you respond to that in terms of a local government and its relationship with the states? I ask you your view: do you not consider that in this whole-of-government approach the knock-on consequences for state and local government would in fact be a diminution of the states' role in the Constitution?

Mr Beresford-Wylie: There are a couple of complicated things there. As I have said, we are not seeking to change the relationship between local government and the states in putting this proposition forward. Local councils came together in a constitutional convention in Melbourne at the end of 2008 and one of the things they accepted was that they were and would remain creatures of the states. They accepted that they would be under the accountability framework of the states. They were not seeking to move outside that framework. In terms of regional development, I would say that local government has been quite strong in its dialogue with the Australian government about the need to make sure that individual councils' views are reflected in the regional frameworks that are put in place. But what is evident to us is that those RDAs are very slimly resourced. They do not really have the resources and indeed potentially the capacity to play a substantive role at that regional level without significant input from local government. It will be local government plans and advice which have a significant influence on the shape of the regional development plans those RDAs are required to produce. Councils are represented on those RDAs. I think that most RDAs have perhaps one or two staff members. They have been in place for a short period of time; they do not have much resources in terms of their administrative ability. Our emphasis has been on making sure that they draw on local government expertise so that whatever they put forward at a regional level reflects the priorities of local communities as they have been brought forward through local councils. So I do not see that those RDAs pose a threat, if you like, to local government and its ability to operate at the local level.

Senator BACK: Do you accept that, whilst local government might have the noble view that it does not want to see a deterioration in its relationship with states and territories as a result of this change, it actually has not got much control over that process?

Mr Beresford-Wylie: I suggest that it does have control and the states have control. I think we have seen evidence that states will respond to the way the federal government deals with local governments; states are cautious to maintain their ability to administer local government. I am not thinking that the states would stand by and watch what has been postulated here as potentially some sort of takeover of local government by the federal government. In terms of local government, we have talked about the fact that local government receives grants from the Australian government but those grants are about 15 per cent of local government revenue. Local government does face significance issues in terms of revenue constraints, but grants are not the majority of revenue that local government have. They are, for most part, a small part of the revenue and in some cases of metropolitan councils a very small part. They are, however, a very substantial part of the revenue received by smaller, more regional and remote councils who are, in a sense, dependent on that grants revenue.

Senator BACK: In the event that this proceeds and, for the third time, is unsuccessful, what strategies would local government have in place to still try to address this imbalance which is so evident and so well explained in your submission?

Mr Beresford-Wylie: We have talked about the fact that all local government will continue to articulate cases with their state governments about the need for adequate resourcing. Local governments have to look at the services they provide and the level of those services and trim their ability to provide those services for the revenue that they have. We have talked about the fact that there is little scope for them to actually exploit rates more fully. There is just a limited capacity there. Local governments do have the capacity to form structures in an attempt to achieve efficiencies. That is why we see the sharing of services across councils. They do try to achieve those efficiencies. There are programs put in place by state local government associations to try to support councils to improve their performance in the area of asset and financial management. That will continue to be the case. That will be an incremental process and it will continue.

Senator BACK: Thank you.

CHAIR: Were the boundaries of these RDAs that have been established discussed with the association?

Mr Beresford-Wylie: Not with the Australian Local Government Association, no.

CHAIR: Do you have a view as to whether they usefully reflect what might be regarded as regional interests?

Mr Beresford-Wylie: They reflect an Australian government interpretation of what those regional interests are—

Senator TROOD: I appreciate that. My question is whether or not that view expressed at a Commonwealth level is shared amongst the members of the Local Government Association in general.

Mr Beresford-Wylie: It is not something that the Australian Local Government Association has commented on or has established a view on, but I will say that local governments themselves have established regional frameworks, regional structures and regional organisations of councils to deal with what they consider to be a regional community of interest for those local governments. Those are the structures they have put in place. On the RDAs, there is a single RDA for the entire metropolitan area of Sydney, for example. There are quite a number of regional organisations of councils operating within Sydney which reflect what local governments in Sydney consider to be their regional communities of interest.

Senator TROOD: You have put your finger on what I see as something of a concern. We seem to have three levels of regionalisation. We have the RDAs. We have what you referred to in your submission—although you do not use this term, but what I would refer to as—organic regionalism, which has developed within states. I think in particular of the examples in Queensland that I know to exist in the south-west corner in relation to the combination of councils involving Barcoo, Diamantina, Longreach et cetera, which is an increasingly strong regional grouping. Then, of course, in most states there are regional boundaries which relate to things like health, education and police districts, and they are all over the place. In Queensland, I think it is fair to say there is no regional boundary that relates to health that in fact accords very clearly with the educational district or the police district et cetera.

So we have these three levels of regionalisation creating, in relation to the idea of regionalism, a great deal of confusion, I suppose. It seems to me that one of the things that might be useful is if someone decided that, if we want to pursue a regional program, we ought to try to rationalise these various levels of regionalisation. I wonder whether you have a view on that.

Mr Beresford-Wylie: The only view I would put forward is that in developing a regional program I think it is useful to build on the existing structures. You are right in saying that a number of different structures exist—catchment management authorities and the regional NRM bodies are further examples of people attempting to create regional communities of interest.

From a local government perspective, though, I do not want to overstate the regional dimension of local government. Local government is created to be local; it is created to look after those local entities. To some extent individual councils will come together and see a benefit from acting slightly more broadly in regional terms and create bodies or share services and do a variety of other things, although they are doing so out of their own initiative because they have a shared community of interest. Not all councils are members of regional organisations of councils. ROCs do not apply everywhere and so some councils do not see that they have that same community of interest with their neighbours.

Senator TROOD: That of course is true, but that kind of regional cooperation may be a strategy which appeals to local government more regularly if the funding and revenue constraints continue to be very strong.

Mr Beresford-Wylie: There may well be a sharing of resources, as we have said. There are some good examples in western New South Wales, around the Orange area, where councils have come together to share

resources to create some efficiencies and some back-office efficiencies as well, but they have not lost their separate individual identities as councils.

Senator TROOD: That is true.

Mr Beresford-Wylie: They can rule that line around what it is that they are doing to achieve the efficiency gains without necessarily losing that identity.

Senator TROOD: That is true in Queensland as well. You made the point about RDAs being underresourced—I think that is the point you were making. Is the association concerned that the absence of resources necessary for RDAs to effectively conduct their affairs might make increasing demands on LGA resources?

Mr Beresford-Wylie: When I say they are underresourced, I listen to the role that has been articulated for Regional Development Australia committees, and it seems a very broad role. To my mind it is a role which, if it is going to be anywhere near achieved, will have to draw on the expertise and input of other bodies such as councils. So it is made in that context. It is entirely up to the Australian government how it wishes to resource those organisations. The emphasis then falls on local government to make sure it is actually having an input and an influence in those RDA committees to make sure that they are, in fact, drawing up local experiences and local priorities when they draft their regional plans.

That is one of the things we have done at an ALGA level: simply going out to our councils and saying, 'The imperative is on you to actually seek out those RDAs and make sure you have an interaction with them and are providing them with the input necessary to meet the responsibilities the federal government has given them.' At the same time we emphasised to RDA officers when they came together in Canberra that, to be perfectly frank, local government is their best friend. Their councils, in fact, are a mechanism and an asset that they should engage with, not a competition. They are not a competitive level of government and not a competitive structure.

CHAIR: We have run over time and have other witnesses, so we will have to move on. Thank you very much for giving your time to the committee today. It has been very helpful. The submission has been very helpful to us. If there is anything you wanted to make reference to subsequently, we would be happy to hear from you, but I do not think we have any questions that we want to put later on.

Mr Beresford-Wylie: The only thing I would say is that we have referred to some research and, of course, to the George Williams opinion on the nature of the Pape case and the things leading up to it. That is available on our website. It is in the public domain if you need to refer to it.

CHAIR: Thank you for your time today. We are very grateful to you for coming.

DOHERTY, Mr Dermot, Assistant Secretary, Commonwealth Grants Commission

SPASOJEVIC, Mr Janko, Secretary, Commonwealth Grants Commission

[12:12]

CHAIR: Welcome. Thank you for attending today. We do not have a submission from you, but I should acknowledge on the public record that when the committee's inquiry began we did seek a private briefing from the Commonwealth Grants Commission which you were generous to grant us. We were very grateful for that. It was very helpful to our inquiries. We felt that some of the issues needed to be on the public record, which is why we have invited you to attend the committee today. We are grateful that you have agreed to accept that invitation. We will allow the opportunity to make an opening statement if you care to make it, and then we will move to questions.

Mr Spasojevic: We have no opening statement.

CHAIR: Mr Spasojevic—

Mr Spasojevic: As we discussed last time, Secretary will do!

CHAIR: I am happy to wrestle with your name, Mr Spa—Secretary! I think it will be helpful to us if you begin by quickly outlining your particular mandate as the Commonwealth Grants Commission and then providing us with some insight into the way in which you undertake the task for which you are most celebrated, which is the work that relates to the GST revenue and the way it is distributed.

Mr Spasojevic: The Commonwealth Grants Commission's main task is to advise the government on how the GST revenue should be distributed amongst the states to leave each state in an equal fiscal position. That is the predominant task of the Grants Commission. From time to time it is asked to do other things, but that is its main role and function. It does that on an annual basis and every five or six years it also reviews the methodology that it uses to reach those decisions. I can talk a little bit more about exactly how we go about doing that, which I think is the second part of your question. To do that, the commission undertakes a comprehensive analysis of the revenues that states raise and the expenditures which they undertake and it asks for each of those revenues or expenditures. We compare that to the average which we have observed—how much more or less than that average would a state need to spend or be able to raise if it followed the average policy of all the states.

Taking payroll tax as an example, the commission looks at the distribution of wages and salaries by state. That is the base upon which payrolls are levied. In a simplified form it would say: if a state had within its boundaries 25 per cent of the wages and salaries, it would be able to raise 25 per cent of the payroll tax in any given year. It goes through this procedure item by item and that allows it to form a view on how much GST revenue a state would need to get to enable it to deliver the standard level of services if it makes the standard or average revenue-raising effort.

CHAIR: When you say 'item by item', do you mean each item of revenue and each item of expenditure?

Mr Spasojevic: Each major item of revenue and each major item of expenditure.

CHAIR: I see. Do you test whether or not it is major by reference to a percentage of overall expenditure or revenue? How do you decide what is major?

Mr Spasojevic: The commission, when it undertook its last methodology review, which reported in 2010, started with the aggregate of all expenditure and asked: how should we break this up? It agreed that it would break something down or split something out if it had a significantly different distribution of the base, so to speak, between the states. So we start with the total and take things out which are very different between the states, leaving a residual item which we think is very much the same between the states.

CHAIR: I am sorry—I have taken you away from your narrative, but it is perhaps useful to explore these opportunities when they arise. Are you able to tell the committee how many items were in that category of there being a significant difference between the states? Can you identify those areas?

Mr Spasojevic: The areas are all identified separately in every report that the commission has undertaken. Each item has its own assessment and it is written up as an individual item, and numbers are produced every year for how we would assist that state for those items. Dermot might know better than I how many revenue items, categories and expenditure there are.

Mr Doherty: There are seven revenue items, of which one is a balancing item, and there are 14 expenditure areas, of which one is a balancing item.

Senator MOORE: Mr Doherty, could you define 'balancing item'?

Mr Doherty: As Jan explained, we started with one revenue category and we said that payroll was different, so we took payroll out and we took another five out, and what was left were all the other revenues we have not separately identified.

CHAIR: Please continue, if we have not completely distracted you.

Mr Spasojevic: That is fine. I think it is better to ask a question as we go along. We undertake these assessments for each of these items of revenue and expenditure. We also make an assessment of states' need to undertake investment and we make an assessment of how much a state needs to save or add to its wealth. At the end of the day we can calculate out how the GST would need to have been distributed in the past to achieve equality. We use those past shares of the GST as the basis on which the future GST should be distributed. We only look at the last three years of history and that enables us to average history and determine an appropriate distribution in the next year. So in February of this year we made a recommendation in relation to the year beginning 1 July. We are six months ahead of the fiscal year in which we are going to apply.

CHAIR: When we had our briefing and you have said this morning that you undertook a review in 2010, I think, which was your most recent five-year review. Is that correct?

Mr Spasojevic: That is correct.

CHAIR: Perhaps you can tell us how significantly or otherwise there was a change in the distribution of revenues as a consequence of that review.

Mr Spasojevic: Before I get to the actual distribution numbers, because you are going to catch me there because I do not have the impact of the 2010 review on the distribution, there were quite significant changes in the methodological approach of the commission at that time which led to significant changes in the way the GST was distributed.

CHAIR: You will say something about that, but I would like to know why it was that you changed the methodology.

Mr Spasojevic: At the end of the preceding review in 2004 heads of treasury engaged in an exercise to simplify the commission's methodology. There was some concern about complexity. There was concern from the commission itself that some data might not be reliable and being asked to carry too much of the load. So heads of treasury engaged in an exercise for some 12 months. At the end of that they identified that simplification of the commission's approach was an important element of any future work of the commission and that was embedded in the commission's terms of reference. The commission then decided that, bearing in mind this desire of the Commonwealth and the states that we should achieve horizontal fiscal equalisation but in a simpler way, it would start with a completely clean sheet of paper in developing its methodology—that is, it would not pick up the preceding methodology and review it and see whether it needed to be changed at the margins; it would actually ask questions from the very beginning. That led it to make some different decisions than it had in the past. One of those decisions was that it wanted to have different states' investment needs have a faster impact on the GST distribution than it had in preceding methodologies. The other decision it took was that it wanted its recommendations to be more contemporaneous, that is to more closely reflect the conditions in the year in which the GST distribution actually occurred. That led it to decide that it wanted to move from taking five years of data in its average to three years of data in its average. Those two things by themselves had quite a significant impact on the methodology and on the final distribution of the GST in that year. So the change from the 2009 update to 2010 was quite significant because of the different treatment of investment and the move from five years to three-year averaging.

CHAIR: Can you clarify for me the extent to which the review that you undertook in 2010 was directed by Treasury? I am interested in the extent to which there was a measure of autonomy that you had in determining the methodology. Was it, for example, the fact that Treasury said, 'Look, it is too complicated. We want you to simplify it and we want you to simplify it around 10 principles, five principles.' The question I am asking here is that one of the criticisms which is constantly made and has been made in the course of this inquiry is that this process lacks a great deal of transparency and we would all benefit by there being a greater degree of access to an understanding of the methodology. Can you address that question about the extent to which the work you have undertaken in relation to this review is a reflection of a direction from Treasury or the extent to which it reflects your own judgement about the best way in which you can distribute this money?

Senator MOORE: Can I add to that as well, Chair? It is 'treasuries' as well, isn't it, because this involves the treasuries of the states? Certainly it is my understanding that this body actually engages in a COAG like process with all of the state treasuries as well as the Treasury from the Commonwealth government. I want to test that and see whether that is an accurate statement as well.

Mr Spasojevic: Let me take the two questions one after the other because they are slightly different. I will get to both of them. The only involvement of the Commonwealth Treasury is via the written terms of reference. They may make submissions, as can any other treasury of the states, but my recollection is that in the 2010 review they made no submission. The only direction we had from the Commonwealth Treasury was the formal terms of reference, which tell the commission to develop the methodology to be used after 2010. It did set out some guidance, but that is formal guidance and there is nothing else apart from that. We were told to make it simpler and we were told to have materiality standards, but we were not told what the materiality standards were or how we were to make it simpler. That very much follows the thinking of the commission itself.

I will now go to the other question. The terms of reference for the commission are discussed with other state treasuries but in the end it is a decision of the Commonwealth Treasurer what he sends to us. How that works you best ask the Commonwealth Treasury because I am assuming they talk to people and modify the terms of reference as they go along. Through the work of the commission we deal quite intensively with the other state treasuries. They make submissions to the commission. We sit down and talk to their officials and the commission responds to the submissions made by state treasuries. That is a very open and public process. We put all state submissions on the internet and all commission documentation is available on the internet.

Senator MOORE: It is working in terms of the way that COAG operates, which is the formal way that the federation operates and how it links in with your group. Certainly it is about getting my head around the fact that direction comes from the Commonwealth Treasurer but in fact the consumer group in a large extent is the state treasuries.

Mr Spasojevic: The stakeholders are very much the state and Commonwealth treasuries together.

Senator MOORE: The information on which you base your calculations comes from states and territories. Is it a separate report they make?

Mr Spasojevic: The primary source of information is from the Australian Bureau of Statistics. It relies on data that the states have provided first to the ABS, which it collates in the form of government financial statistics.

Senator MOORE: Which are special reports that the states give to stats for this purpose?

Mr Spasojevic: Which states give to the ABS?

Senator MOORE: Yes.

Mr Spasojevic: Not because of what we do. It is part of the ABS statistical process to report on the financial statistics of the Commonwealth, state and local governments. They collect data from all of those bodies and publish it. It is our primary source of data. We do collect some data specifically from the states in areas that the ABS does not collect and they report to us on the basis of the data requests we make of them.

Senator MOORE: Are they standard requests? I am trying to see what the basis of the model is. We have the stats information and the requests of the states to provide further information. Are they standard request from the states?

Mr Spasojevic: They are standard in that every year we update the numbers, so every year we go to them and ask them for the numbers that relate to the most recent financial year and any changes to preceding financial years. So there is a standing process which occurs on an annual basis.

Senator MOORE: And they are free to make other submissions as required in terms of the process, which people have done over the years about their perceived inequities. They put a formal submission in to you.

Mr Spasojevic: Absolutely.

Senator MOORE: The Prime Minister has announced a review.

Mr Spasojevic: Correct.

Senator MOORE: Will that review be done by you?

Mr Spasojevic: No.

Senator MOORE: I want to get it all on the record.

Mr Spasojevic: A completely independent review has been commissioned by the government.

Senator MOORE: Of the whole process?

Mr Spasojevic: Yes.

Senator MOORE: That is for completion this year?

Mr Spasojevic: I think there is a draft report next February and a final report the following August.

Senator MOORE: And that review is looking at the whole way the system operates?

Mr Spasojevic: Yes, I think that is probably the right form of words.

Senator MOORE: Thank you.

Senator RYAN: I was not present at the private briefing last year, I was away, so my apologies if part of this was covered. With respect to what you described before as the average policy—for example, on payroll tax, the amount that could be collected—can you list what the other revenue measures are? You said it was payroll tax and five others that you looked at. I am more familiar with it before simplification, I have to admit, so sorry if I get it wrong.

Mr Doherty: Payroll tax, land tax, stamp duty and conveyances, insurance taxation, motor taxes, mining revenue, and then 'other revenue'.

Senator RYAN: As an example, the state of Western Australia does not have pokies outside its casino, as I understand it, as opposed to places like Victoria or New South Wales where there are a lot more. Is Western Australia effectively penalised in terms of GST disbursements for not raising as much money from gambling machine revenue? It does collect below the average of what it could collect if it had the same number of machines per capita as the other states.

Mr Spasojevic: Gambling is a good and a bad example of the question I think you are trying to ask. If I could think about land tax for a moment, the Northern Territory does not collect land tax, but we calculate how much they could raise if they had the average land tax rate of all the states and that assessed calculation is what is used to determine their GST. So the fact that they choose not to generate any land tax does not lead them to have more GST revenue.

Senator RYAN: Exactly. So how does gambling work? It is contentious, for the reason I used.

Mr Spasojevic: The reason I did not want answer in terms of gambling is we make no differential assessment of gambling.

Senator RYAN: It is not considered the way you just described land tax?

Mr Spasojevic: It is not considered as it forms part of 'other revenue' and we consider that the states can raise an equal amount per capita of those taxes and charges.

Senator RYAN: Sure.

Senator BACK: Can I just clarify this, because revenue for some of the states is 13, 14 or up to 15 per cent from gambling. I am still not clear from your response to Senator Ryan's question if Western Australia is advantaged or not advantaged by—

Mr Spasojevic: It is unaffected in terms of its GST distribution.

Senator RYAN: In simple terms, it is not paid more GST because it is unable to raise the gambling revenue—

Mr Spasojevic: Correct.

Senator RYAN: and it is not paid less because it refuses to.

Mr Spasojevic: Correct. Gambling revenue currently has no impact on the differential distribution of the GST.

Senator BACK: Are there other examples? Gambling is one.

Mr Doherty: There would be one-off revenues that states may raise which we would put in this 'other revenue' group.

Senator MOORE: Would that be like a privatisation? As a one-off revenue that would be a significant income. Various states over the years have privatised certain things.

Mr Spasojevic: Privatisations are not treated as revenue. I believe that is a balance sheet transaction.

Senator MOORE: So it is not counted as revenue for the year in which they get the money?

Mr Spasojevic: I think that is right.

CHAIR: Colleagues, I think we should let Senator Ryan proceed with his questions.

Senator RYAN: You used land tax as an example. Unlike payroll tax where, say, you have 25 per cent of the payrolls, land tax is a harder thing to measure easily because you have to make assumptions about the value of

land, I suppose. States do this to varying degrees of competence, I suppose, with irregular or regular assessments. Obviously, with the land in Sydney around the harbour, I would suggest the government of New South Wales has much more capacity to raise land tax than the government of the Northern Territory would, even though it chooses not to, or the government of South Australia would, even if I considered it on a per capita basis. So, when you look at the capacity of a state to raise revenue, New South Wales has more capacity per capita to raise revenue on land tax than does South Australia because of the value of land. Does that mean that, in the way you make your assessment about the disbursements of GST revenue, New South Wales should be raising more per capita from land tax than a state with lesser capacity like South Australia in order for the GST disbursements to be unaffected?

Mr Spasojevic: I will try to go through that question to make sure I understand what it—

Senator RYAN: Please.

Mr Spasojevic: Let me make two statements which I think you said were assumptions. Let me assume that New South Wales has a higher value of land per capita and South Australia has a lower level—

Senator RYAN: Than New South Wales.

Mr Spasojevic: than New South Wales. What we would say is that, at an average land tax rate, New South Wales will—

Senator RYAN: That is an average across the Commonwealth?

Mr Spasojevic: An average across the Commonwealth. At an average land tax rate, New South Wales will be able to raise more land tax per capita than South Australia.

Senator RYAN: Yes.

Mr Spasojevic: Other things being equal, it would therefore get less GST per capita.

Senator RYAN: So if New South Wales chose to reduce its per capita land tax rate to that of South Australia then the truth is that it would end up worse off in net financial terms because it would not get extra GST revenue to compensate.

Mr Spasojevic: I will put aside any effect on the average, because New South Wales is 30 per cent of the average, so there would be an effect, but the thinking becomes difficult then—or more difficult. If the average were not changed, the decision of New South Wales to raise less than the average is a cost it bears itself.

Senator RYAN: Exactly. This is where I wanted to get to the point. It is possible, under the arrangements that are currently in place and have been in place for a long time, for the relativities as they are calculated—the capacity to raise revenue—actually to mean that the burden on individuals, because we look at it per capita, can be higher in some places than in others to pay tax. So in order to maintain an unaffected GST distribution—if we exclude the impact on the national average as you outlined, Mr Secretary—South Australia, if land values are less per capita, will be paying less land tax than New South Wales citizens.

Mr Spasojevic: Yes.

Senator RYAN: I think that is a very important point.

Mr Spasojevic: I think what you have asked is: if every state levied average tax rates, would people in areas of low land tax pay low land tax?

Senator RYAN: The point I am making, though, is that this is so widely not understood—I am not saying misunderstood. It is not the easiest part; I studied it and I still have trouble getting my head around it. It is still based upon people in different parts of Australia on an issue like land tax, which is different to an income based tax like payroll tax. Citizens can own a quarter-acre block in Sydney, subject to land tax, or a quarter-acre block with their home in Adelaide, subject to land tax. This system assumes and depends upon the citizen in New South Wales paying a higher amount of tax on their quarter-acre block.

Mr Spasojevic: It assumes they pay the same rate of tax.

Senator RYAN: Exactly, but because we have some—

Mr Spasojevic: So they bear the same burden.

Senator RYAN: We have immovable economic commodities like land tax—unlike payroll tax, which can move with labour. There is a different burden that falls. Many years ago, the Kennett government when it was first elected introduced a levy of \$100 per rateable property; it was called the state deficit levy. It was in place for three years, I think, from 1993 until 1996. I was a bit younger at the time; I was still at uni. I recall from when I was studying this that when the Kennett government removed that levy it was then penalised—this was pre GST, but there were FAG relativity disbursements. The then Kennett government effectively suffered a penalty in its

disbursements under the financial assistance grants because it had raised a tax and was now effectively choosing not to. It had a taxing capacity that it was not actually using. I know that goes back a long way, but I was wondering if either of you had memory of that or whether the model that I am explaining would still happen today. If a state introduced a tax for a number of years and then chose to withdraw it, would that in effect impact upon the calculations that you are talking about and penalise it, for lack of a better way of putting it?

Mr Spasojevic: I think you are going to test our memories to go back to Kennett.

Senator RYAN: I tested my own, so I am not—

Mr Spasojevic: You are going to test mine, because I only joined the commission in the 2000s, so I certainly cannot answer that question.

Mr Doherty: I will take it under advisement, but I believe we put that tax, because it was a tax by one state only, in the balancing item, and therefore it did not affect the disbursements of any state.

Senator RYAN: Not even Victoria?

Mr Doherty: Not even Victoria.

Senator RYAN: But the principle could apply, could it not—the principle of a state having a source of revenue, having raised a tax from that source of revenue and then discontinued it, then finding itself in much the same situation? It may have been a Kennett tax in Victoria, but it could be any state doing the same thing with the same consequences.

Mr Spasojevic: By and large, if one state introduces a tax it does not constitute average tax policy so it has no impact on what the commission does. It has to be something which affects either the majority of the tax base across the country or the majority of the people in the country. If New South Wales were to introduce a tax that no other state had, we would just say it is following some very different policy and it should not affect the GST distribution.

CHAIR: So it would not affect the distribution while the tax is being raised? If it were discontinued, it would not affect the distribution either?

Mr Spasojevic: That is correct.

Senator RYAN: That is very helpful. When you are calculating what I understand used to be called 'disabilities' with respect to spending—I might be going back to un-PC or old language with this but I can remember a story about calculating the relative spending requirements to support public transport in the various states and territories. Again, this was 10 or 12 years ago, so dismiss it if it is either apocryphal or out of date. One of the things I heard at that point was that the ACT received a spending bonus because they had a spending disability. There was so much free car parking around so many workplaces within Canberra as opposed to Sydney and Melbourne, where more people were simply funnelled onto public transport, that, in essence, it was going to be more expensive for the ACT to maintain a mass transit public transport system. Is that the sort of story that is apocryphal or is that the sort of story that could fit into the guidelines in which you operate?

Mr Spasojevic: It is not apocryphal but it does not exist anymore.

Senator RYAN: It used to?

Mr Spasojevic: It used to.

Senator RYAN: That is also very helpful.

Mr Spasojevic: It was simplified.

Senator RYAN: When you look at something like health—and you talked about the average service delivery of health—what do you use as your measurements? Life expectancy takes years. Do you use input measures like the number of beds per hundred of population? Do you use the number of GPs per head of population? How do you decide that the people of Queensland need \$1.20 to provide the same health service for which the people of Victoria might need 88½¢?

Mr Spasojevic: We use the Australian Institute of Health and Welfare database. They give us data based on the spending on different types of people by their demographic and social characteristics. If you are an 80- to 85-year-old Indigenous person, we know what the average spend on such a person is across the country, for example. We say that if that is what is spent on average on those types of people then to deliver the average service that is how much the average state would need to spend. We do not look at the measures like GPs.

Senator RYAN: That makes perfect sense.

Mr Spasojevic: We look at how much the states—

Senator RYAN: Doesn't this then have an anticompetitive aspect? If you are always pulling everyone back to the mean, the average spend, then Victoria, for example, could prove that if it got its cost per head down it would effectively then suffer a funding penalty absent of the impact upon the national average?

Mr Spasojevic: No. You are completely wrong there. If I assess that you need to spend the average of \$100 and you can do it for \$80, that \$20 is your money to spend as you see fit.

Senator RYAN: But then, if I am, say, a state like New South Wales and I start spending \$120 instead of \$100, I am going to have a significant impact on the national average, dragging costs up, aren't I?

Mr Spasojevic: Correct.

Senator RYAN: That is something that you do not take into account?

Mr Spasojevic: We do not take that into account. We assume that the average spend is the average spend and incorporates the average level of service delivery efficiency.

Senator MOORE: You make no assessment of whether that is the right level or the appropriate level? You do not make any qualitative assessment; it is purely quantitative?

Mr Spasojevic: The commission make no judgment about what states should spend their money on or how they should raise their revenue; we just look at what they do, and it is purely quantitative in that sense.

Senator RYAN: The Northern Territory is a classic case. It has a significant Indigenous population. The health costs for Indigenous people are significantly higher. It therefore gets significantly more per head than does the state of Victoria or Tasmania. Those grants are then given as untied, aren't they?

Mr Spasojevic: Correct.

Senator RYAN: Even though the Commonwealth Grants Commission says the Territory gets \$3.20 rather than a \$1.20 to spend on health because of the balance of its population demographically and that money is given to the Northern Territory, just to clarify, that money is not tied to the purpose for which the disability is calculated?

Mr Spasojevic: Correct. Once the GST is determined, it is a lump-sum transfer to the Territory to spend as it sees fit.

Senator BACK: Could you give us a breakdown of the per capita GST return to the states and territories in percentage terms?

Mr Spasojevic: For the coming financial year?

Senator BACK: Yes, or the current and the coming if you have got them.

Mr Spasojevic: I have got numbers but they may not be right because the amount of GST keeps changing all the time. Do you want them in billions?

Senator BACK: Per capita per cent.

Mr Spasojevic: I can give you the shares of the GST.

CHAIR: Senator Back, would it be helpful if we had a table on this, or do you need some of this information now for the purpose of your questions?

Senator BACK: I do not need it right now to continue my questions, no.

Mr Spasojevic: It is publicly available in the published reports. Table 2 on the executive summary of the 2011 update gives you the state shares. The state shares per capita are what we call the relativities, and that is in table 1.

Senator BACK: Thank you. I can source that. You mentioned very kindly the revenues. I think you said there were 14 expenditures including one balancing. Do the summary of the expenditures appear in the reports also?

Mr Spasojevic: Yes.

Senator BACK: The Northern Territory Speaker and her opposite number appeared before this committee in Brisbane and they were pleading the case for statehood. I recall asking them, 'In the event that the Territory achieves statehood, to what extent would this actually improve their financial position vis-a-vis the GST share per capita that it gets?' They said, 'It wouldn't at all.' I said, 'Don't you have an objective to get closer to being self-sufficient?' They said, 'No, why would we?' So I ask you the question.

Mr Spasojevic: We treat the territories as if they are states.

Senator BACK: Sure; I understand that. My question is in relation to all eight. You have explained to us the averaging, you have explained to us the need for horizontal fiscal equalisation, but can I ask you: where is the incentive for states and territories to actually maximise revenue or contain expenditure for the overall good of the

nation? Why? If one state—Tasmania, for example—in the current structure chooses, for whatever reason, to not proceed with or to maximise their revenue opportunities in one particular area, where is the incentive for them to do so? They are getting a good share. They might say they are not, but others would say they are. I suppose it comes back to the question Senator Ryan asked. It is not so much in relation to competitiveness. But it is not clear to me where in the guidelines the states and territories should be aiming to act as responsibly and effectively as possible to maximise revenue and contain expenditures.

Mr Spasojevic: I think those constraints fall outside the gamut of what the commission is asked to do, in that if we think of the states collectively we are asked to distribute a given amount of money amongst them. We are not asked, for example, to determine what a good state policy or a good state fiscal position is and distribute the GST to somehow make that happen. We just give them all the same fiscal outcome. You may think that the states should have a tighter or lower average outcome. It is beyond the commission to comment on whether that is appropriate or not.

Senator BACK: You did make the observation that one of the changes being contemplated—I think you mentioned two—was a five- down to three-year reduction. The first that you mentioned was the taking into account of the different investment needs of the different states. Can you explain to me the basis upon which those decisions and calculations were made? I would have taken that to mean that a particular state might have a greater or lesser investment need. In turn, in the event of a greater investment need, that might actually return more to the Commonwealth as a result of that investment being made. Am I wrong in that assumption?

Mr Spasojevic: I think you are wrong in drawing the conclusion that we do not look at the financial return to any particular body. We have a very different way of looking at investment. The way the calculations are done is that the average state needs the average amount of infrastructure—if you can imagine that concept—per person. That average amount of infrastructure is determined by the decisions of all the states collectively and basically what we do is we say that states which have fast growing populations will need to spend more than the average to give them that average level of infrastructure. It is their faster population growth which drives our decisions on how much investment they need to take.

Senator BACK: If it is not then within the commission's purview to consider the question I was asking about the effectiveness of operations of states and territories, whose is it? You know the state I come from and you probably know the comment that our premier made recently about Tasmania being a national park. Who then should take that level of accountability and responsibility in making the final determination?

Mr Spasojevic: I think that is a very good question but I do not know what the answer is myself.

Senator BACK: Sure. I know time is against us so therefore I will ask one final question. You did hear the chief executive of the Local Government Association giving his evidence to us earlier. Can you explain if at all, how the commission takes into account this need of local government in terms of your GST calculations or indeed are they just simply drawn up as part of your overall averaging process?

Mr Spasojevic: The functions of local government fall outside our ambit. We only look at the functions of state general government. We do not think about local government itself. The only way that there is an impact is any state government spending that they direct towards their own local governments. I think it has almost no impact at this point in time.

Mr Doherty: I think that is correct.

Mr Doherty: We make no differential assessment of what a state needs to do to support it.

Senator BACK: They cannot appeal to you for this widening gap between the services they are expected to deliver and the funding that follows?

Mr Spasojevic: No, I am sorry. It is not something that currently is treated by the methodology because we consider it falls outside our ambit.

CHAIR: Were you asked to undertake the task, is it theoretically possible to do the same kind of calculation that you do for states amongst the local government areas across the country?

Mr Spasojevic: I think in the past the commission actually was asked to do that.

Mr Doherty: In 1974 and I think 1975 we were given that task. It now falls to the local government grants commissions and there is seven of those in each of the states except the ACT. They do that task for the money the Commonwealth passes to the local governments.

CHAIR: When you undertook that task did you undertake it on more or less the same kind of basis of principle that you undertake the task in relation to states?

Mr Doherty: We did. It preceded my time at the commission as well but it was on the same approach.

CHAIR: Mr Doherty, is it your understanding that that continues to be the approach that the commission undertakes now?

Mr Doherty: When we did it we would have used a national average but I believe that when the state local grants commissions do it they use a state average.

CHAIR: They do it independently for their states?

Mr Spasojevic: Correct.

CHAIR: It is not necessarily coherent or nationalised, as it were, across the country. Is that correct? Are they applying common methodologies in each state?

Mr Spasojevic: The Commonwealth money for local government gets distributed amongst the states into eight pots, according to how many people there are in each state. Each of those pots is then divvied up to try to equalise the standards of local governments within that state. There is no assurance that the standards are therefore evened out nationally.

CHAIR: So there could be significant differences between the revenues received from local governments in one state as distinct from others, even though they might be applying the same kind of methodology?

Mr Spasojevic: Correct. For example, even after the money is distributed, local government in the Northern Territory—where only half a percent of the total goes—probably has a lower fiscal capacity than local government in, say, Victoria where 25 per cent of the money goes.

CHAIR: Was that the outcome when you undertook the task, Mr Doherty? Or was there a more representative return to government—a more equitable return, given their status across the country?

Mr Doherty: It was 10 years before I was at the commission so I do not know what the outcomes were.

CHAIR: In relation to the review that is being undertaken, following on from the question from Senator Moore, it is not a review that you are undertaking but are you expecting to make a submission to the review? Presumably you have some role in the review and I just want to understand how that works.

Mr Spasojevic: Staff from the commission will be seconded onto the secretariat of that review, which is being provided by the Commonwealth Treasury. The review itself is being undertaken by Nick Greiner, John Brumby and Bruce Carter. They are the three reviewers supported by a secretariat from the Commonwealth Treasury, which will have state and commission staff seconded onto it. The commission has said that it, first of all, welcomes this review and thinks that this is an important issue that needs to be addressed. The review basically reviews the commission's own terms of reference, which it has always thought exceeded its own abilities but it has called in the past for such a review to occur in the country. The commission will be as helpful as it possibly can in providing information and briefing to that review but it is not clear that it will make a submission because it would be making a submission on its own terms of reference, which it thinks is probably not appropriate. So it will be as helpful as possible without necessarily making a submission.

CHAIR: I can see the awkward situation you are put in. Do I take it, though, from your remarks that you have been uneasy with the terms of reference that you have received consistently?

Mr Spasojevic: No. In the most recent 2004 review, there was a great deal of concern by some states about whether fiscal equalisation itself was the right thing that should be occurring, but the commission has never been asked that question. It has been asked, 'Can you tell us how to implement HFE?' The commission at that time said: 'The question of whether there should be HFE is a question for government. It would be appropriate for the government to have a review of the question and then tell the commission what it wants it to achieve.'

CHAIR: I think I am right in saying that this is the most sophisticated means by which any federation seeks to achieve horizontal fiscal equalisation amongst its elemental parts. Is that correct?

Mr Spasojevic: I think that is a fair statement. From what people in other federations tell us, we have the most sophisticated and involved system.

CHAIR: And complex, it would seem, as a consequence?

Senator MOORE: Less complex than before, I believe.

Mr Spasojevic: Complexity is a very interesting question. It would be much simpler if the states were simpler. If the states were all homogenous our job would be made a lot easier. Our job is made difficult because the states are so different and they engage in such a wide range of activities and tax-raising functions. I believe our complexity mirrors the complexity of the real world.

CHAIR: Thank you for your time. It has been most interesting and we are very grateful to you for returning to the committee and providing your evidence in the public domain.

Proceedings suspended from 12:59 to 13:49

GALLIGAN, Professor Brian, Private capacity

CHAIR: It is good to see you here, Professor Galligan. We have received a submission from you, submission No. 46. Do you wish to make any amendments to that submission at this stage?

Prof. Galligan: No, thank you.

CHAIR: I now invite you to make an opening statement, after which the committee will ask you some questions.

Prof. Galligan: Thank you for inviting me to the committee. Apologies for getting the written pieces to you a little bit late. I sent a paper, which I understand that you got, which summarised in a sense many of the things that I would have said about Australian federalism had I had more time. You have that to look at. Then just a couple of days ago I prepared a shorter summary directed more towards the specific heads that this committee has been asked to examine. I will speak very briefly to that. I understand that that has been circulated as well.

The first point that I make regarding your point a, the issues and priorities for the reform of relations between the three levels of government, is a fairly obvious one: many of the significant major policy areas have multiple dimensions, international as well as national, state and local. The Australian Constitution, which captures essentially the national and the state part, is appropriate generally for handling the sorts of policy complexities that we are facing now and that we are likely to face.

The main aspect of Australian federal development over the last decade or so—although this has been corrected, as I make clear in both of the papers—is the propensity of the Commonwealth to get involved in ever more areas that would have been traditionally and formally are state constitutional matters, such as aspects of health, education, infrastructure and so on. Commonwealth leaders, and I cited Mr Howard's aspirational nationalism, either have little respect or little positive appreciation of Australian federalism. The Commonwealth, because of its excess fiscal powers, has the money to bankroll this. The point that I make, though, is that the particular balance in Commonwealth-state politics is one that is determined—although it has a constitutional base—very much from time to time by the balance of politics, intergovernmental relations and particularly the combinations of competition and cooperation that occur throughout many of the policy areas.

I have suggested that there are areas that could be reformed, but these are mainly within the sub constitutional and intergovernmental area. In particular, COAG and its operations could be strengthened. We should also have much more attention not just on each level of government managing its own policies in very specific programs but managing intergovernmental programs. It is surprising that we do not seem to have this public administration focus in the literature and certainly not in the practice in Australia. So there is a need to develop a whole approach to intergovernmental management.

On the distribution of constitutional powers between the Commonwealth and the states, I have argued very strongly that this should be left alone. There is no need to tamper with it. It is unlikely that any tampering would succeed by way of constitutional amendment anyway.

The powers in the Constitution for the Commonwealth are very broad. They have been interpreted ever more broadly by the High Court. If one combines that with the fiscal power of the Commonwealth, there is virtually nothing that the Commonwealth could not do. In fact, a federalist would probably be more interested in pegging the Commonwealth back, but there is not much prospect of doing that constitutionally because the Commonwealth controls the powers. And it is not necessary anyway. I think there are some issues with financial relations that need very serious attention. I have just signalled one of them. I have supported the rather comprehensive equalisation arrangements that we have but suggested they could be much more transparent. I remember in my days here at ANU organising seminars on the Grants Commission. You could hardly find anybody who was not an insider who knew really how to talk critically about what the Grants Commission was doing. There are issues. For example, a lot of money in the equalisation process goes to compensate particularly the Northern Territory for providing services to isolated Aboriginal communities but of course the Territory in respect for the principle of state and territory sovereignty does not have to spend that money in the areas for which it has a disability and gets it. It can spend it on a flash parliament house overlooking the Arafura Sea.

On constitutional amendments, I have suggested that it is not really the way to go. It is unnecessary and they would be unlikely to succeed. My view is that the Australian people are actually fairly smart, they are not stupid, and the main reason we have a bad constitutional record is that Commonwealth governments put up proposals that are bound to fail or they put proposals up that have been put before or that there is no general agreement on.

COAG I have suggested should be a major area for reform. Regionalism has been getting a run from some of my friends and colleagues, regionalism in the sense we have it in a fairly strong form with states. Some would say they are too large but nevertheless they are big regions. We have it in a micro sense, particularly with amalgamations of local governments. I think of my home town of Dalby. Probably not too many of you know Dalby, a country town. The amalgamation of local councils to create a larger Western Downs, or whatever it is called, means that there is a local government authority now in control of a much larger area which is much better equipped not only to handle floods but also gas and coal developments and so on. Then if you look at any major policy area you find that there is often a myriad of arrangements, some of them regional, between state and local governments, either formed by local governments or formed by states or formed by the Commonwealth for specific purposes in specific policy areas.

Finally, and I suppose this is the sort of optimistic one, if we are thinking about federalism a nice way to think about it is that the 20th century was nation-building and consolidation, and certainly we have had that in Australia. In the 21st century the larger structural pressures will be towards more globalisation and more localisation driven by democratic demands, so the propensity of Australian government to centralise things I think will be increasingly out of step and one might hope that in the future it might be wound back.

CHAIR: Thank you very much, Professor. I would like to begin with that last point you make because it is a point that has been made to us on other occasions when we have been taking evidence. It seems to amount to this, that federalism as a system of government is likely to be more relevant in the 21st century than a unitary system of government. In other words, the virtues of federalism better respond to the points you made here than any other system of government. Is that a fair proposition, do you think?

Prof. Galligan: That would be my view and I think it is very speculative and of course countries can go different ways and play things differently. The reflexivity of institutions means you can do things the same way with different institutions or differently with the same institution. But if you think of what is happening in Europe, clearly a complicated system of governments and subgovernments and a strengthening of non-national governments is really the standout factor, also if you think of Great Britain and Northern Ireland. I think the structural forces will be going in that direction. That is not to say that we will necessarily go that way but I think one could say that the atmosphere or the circumstances, the larger environment of the 21st century, is going to be much more congenial to federalism. You would not know that looking at the current Commonwealth leaders or National Press Club.

CHAIR: I think that is absolutely correct. In fact, some of the evidence we have received as a committee is at odds with the prevailing wisdom that exists in political circles about how the Commonwealth should evolve. The point that seems to come through most of your writings is that there is a need for reform of the Federation in various ways and you have just outlined some of those. The further point that seems to follow is that much of this can be done without necessarily undertaking constitutional reform. In other words we ought to be looking elsewhere for the means by which we can actually repair the Constitution or, if you do not like the word 'repair', at least make it more relevant to Australia's needs in the 21st century. Is that a fair proposition as well?

Prof. Galligan: It is very interesting. If you go to America they say, 'Our Constitution is 200 years old'—I was there during their bicentenary—and so it must be good.' In Australia they say, 'It's 100 years old, so we must need a new one.' I suppose it is part of the political culture which is 'progressive' in a fairly superficial way. There is nothing that you would want to do that you cannot do without constitutional change. I actually think that the Constitution is pretty robust—it has been shown to be that through the 20th century. I think it can be adjusted virtually in any way you would like under existing arrangements. There are some exceptions like republicanising the head of state.

The other factor is that you do need to have a weighty reason for changing the Constitution, particularly the federal arrangements for the division of powers. It is very difficult for those amendments to get up. It is pie in the sky for the most part and it is really going down the wrong track. Constitutional lawyers professionally if there is a problem say, 'Let's fix the Constitution.' The problems are not constitutional problems. There is a tendency towards what I call 'coordinate federalism'. Some people think that a federal system should have separate and distinct governments with separate and distinct responsibilities—'You have that, we have that'. That is simply wrong. Yet so much of this talk about reform is in terms of sorting these things out. That is a very simplistic, mentally incorrect view.

CHAIR: Is that the force of your observation in your submission about the need not to 'fiddle'—a very elegant term I think—with the distribution of constitutional powers?

Prof. Galligan: Yes. I have developed that at any great length in the paper and in some of my other writings but I think it is (a) unnecessary and (b) it is unlikely. You could pretty much put your money on it; it will not

work. There will be enough people who will take an opposite view. I have not seen any good proposals yet as to what you would do except some suggestions to facilitate the sort of sharing—I think you can do that already.

CHAIR: But you do say, do you not—I just cannot find the reference to it—in relation to heads of power like health and education that perhaps the Commonwealth has intruded too far into those areas and they ought to be retrieved for the states' responsibility.

Prof. Galligan: You can do that without constitutional change just as you have done it as it has developed this way without constitutional change. The High Court has been complicit in developing very expansive Commonwealth powers although not completely unlimited as the Pape case showed. It seems to me that the drivers for this will not be constitutional proposals but they will really be—and I think we are witnessing some of it at present—the cycles of Australian politics. Give the Commonwealth enough policy rope and it will sort of hang itself. It will stuff up on enough policy areas and you can see it. It did not work for the Howard government, they lost office despite saying, 'We'll take over this, we'll take over that and we'll send the army to the Northern Territory,' and so on. It did not work for Kevin Rudd who was going to take over the hospitals—I do not know why you would ever want to do that. They are difficult to run and it is not because of the federal problem it is because of hospitals, they are difficult to run all over the world. We have this easy tendency in Australia to think 'We have a problem with health, we have a problem with water in the Murray or a problem somewhere; therefore it is a federal problem.' It is not. I think that the political cycle and political leadership will have to address these things otherwise there is not much chance of them being developed. If you went back five years, one would have been rather pessimistic, because all of the forces seemed to be towards concentration of Commonwealth powers—Mr Howard riding high on his aspirational nationalism. At this point in time one would have to say that it is not likely that we are going to have this same thrust, with the Commonwealth taking over this, that and the other thing. Rather, in the states we increasingly have new governments that are going to be more assertive.

If Commonwealth public servants and advisers actually thought seriously about roles and responsibilities, they would want to get the Commonwealth out of a lot of the silly things that it is getting into, like paying teachers bonuses and things like that. How does it know which teachers to pay bonuses to; it does not know.

CHAIR: You made the point, on that theme, that politics has delivered us into that position, but so too has the High Court.

Prof. Galligan: Exactly, yes.

CHAIR: Whilst we might have a change in the cyclical nature of politics, we have all been waiting for 100 years for a change in the attitudes of the High Court, and it essentially has not come. Do you anticipate that that might change as well? And the important thing is, can the rebalancing of the Constitution be achieved without the High Court accepting that that is part of its responsibility?

Prof. Galligan: I think it can. I think what the High Court has essentially done is deal itself out of the federal adjudication balance of the roles of government for the most part and essentially left it to politics. Just because the High Court gives a very expansive definition of external affairs power or the corporations power does not mean that a Commonwealth government is going to take that up. It really depends on the political opportunity, the political drivers, the political leadership, the mood of the nation at the time and the strength of the states.

A committed federalist might think it is a good idea—and if Senator Ryan were here he might think it is a good idea—to have a constitutional amendment to peg back the powers of the Commonwealth and to, in a sense, perhaps instruct the High Court to get rid of Engineers methodology, which is an inappropriate way to interpret a federal constitution, and come up with something a bit more sensible. That is unlikely. But, because of my confidence that you can do it through politics, it is probably unnecessary.

CHAIR: We had evidence before the committee at our Perth hearing, I think it was, from some academic colleagues of yours along the lines of there needing to be some kind of constitutional amendment that reminded the High Court that the document they were interpreting was in fact a federal document.

Prof. Galligan: They know that.

CHAIR: The point seems to be that they may well know it but they are not paying much attention to it.

Prof. Galligan: Some of them are. If you look at the Work Choices cases on the corporations power, the strange combination of Callinan and Kirby giving very strong and eloquent articulations of a federal constitution. If you go back to the Tasmanian dam case earlier you will find the same from the then Chief Justice Gibbs and so on. It is not that they do not know about this; it is that they do not accept it. A lot of them come from Sydney or they come from a background where they do not have a sympathetic understanding or acceptance of federalism. They stick with this Engineers methodology.

Senator MOORE: You said that Australian federalism is currently being tackled by COAG, and that is where the effort and attention should be and that is the current model we have got. What kind of effort and attention should we put into COAG?

Prof. Galligan: If COAG is going to be a first order federal institution it has to have a much more robust and self-sustaining institutional base. Look at the institutions in Australia that are strong: the ACCC, the Productivity Commission and the Grants Commission are all strong. If you look at those institutions you can see that they all have substantial and good staff, whereas I think this is run out of Prime Minister and Cabinet or somewhere there. If you could establish it as a genuine collaboration between the governments, staff the office properly and give it some really significant research and policy development functions, that would be one thing. But it really does depend on political leaders acknowledging that that would be a good thing to do. One of the obstacles, particularly from the Commonwealth's point of view, is that, if you strengthen that, you would tend to lose some of the Commonwealth's dominance in talking it up or talking it down from time to time. So I think it would only work if it were part of a more robust federal consensus among political leaders that you do need a substantial intergovernmental institution to support genuine intergovernmental discussion and policy development and management.

Senator MOORE: So, basically, it is resourcing?

Prof. Galligan: Resourcing is a pre-requisite, but I think it does require political consensus among political leaders that, in a federal system, you do need some sort of intergovernmental institution or body that is sufficiently strong and has the capabilities to support intergovernmental decision making.

CHAIR: Do you mean that in the sense of being a separate agency—such as the ACCC, for example?

Prof. Galligan: Not necessarily an agency, because it is probably too highly political for that, but at least having coordinated state as well as federal input and not just something that is done by the way, in a sense, by PM&C or a branch in PM&C.

Senator MOORE: You said that you need that political commitment and engagement at the state and federal levels. How do you think the current state and federal leaderships view COAG?

Prof. Galligan: If you take it a little further to the more immediate time span, I think it is very interesting. Take Mr Howard, for example: he started off with the GST, I think, and his dealings with the state premiers in the earlier part of his prime ministership were very positive. But, then, as his electoral and political needs and perceptions changed, he changed in his view and approach. So, instead of working with this whole wall of state Labor premiers, as he did in the earlier time, he decided that the political advantage was to work against them, to blame them, to criticise them and take over areas and so on.

Similarly, you can see fluctuations in Labor prime ministers. Rudd came in very much with this cooperative federalism notion but, then, increasingly it was, 'We're going to dominate.' Currently I think we have a very weak national government because it is a minority government; it does not control the Senate and all those sorts of things, as everybody knows, and it is not likely to be able to do much, or want to do much, at all on the federal front. Until this new cycle of elections, we have had rather longstanding and tired Labor governments that were battling just to stay on track. So I think we are coming out of a period of the Commonwealth calling the tune and into a period where the Commonwealth will not be able to and cannot.

There will be much more political competition and whether that will lead to a more consensual view—I think we are still waiting for the Commonwealth and Commonwealth advisers to say, 'There are certain things the Commonwealth shouldn't do.' If you go to Canada and look at education, you will find that their national government does not get involved with schools at all, basically; yet, their school system is better than ours. I do not know why Australian political leaders and bureaucrats and advisers do not twig to this more, that there are certain things we do not want the Commonwealth involved in, that we want them to get out of.

Senator BACK: Can I start with the High Court. I think I shock the chairman every now and again when I make the observation that I think the High Court would be eminently enriched by having one or possibly two nonlawyers on it.

CHAIR: A veterinary scientist, perhaps!

Senator BACK: No, I do not think a veterinary scientist at all; just people of eminence and with the wisdom and experience of a variety of life. But I will not ask you to comment on that. What I will ask you to comment on is that you mentioned globalism, localism and, to use your term, 'glocalism'. Can you tell me, in the way the High Court is currently structured, whether it will assist, have no affect or in fact adversely affect what you believe is the way of the future?

Prof. Galligan: The High Court is clearly very important, but then there is the question of whether it really leads or whether it follows. In very important ways it follows in that it decides only the cases that come to it, and it is a bit happenstance as to what comes to it. Many things can go on for a long period of time. For example, the offshore jurisdiction was not settled for a long time. With governments working together and working things out, it is only when they come to something that they cannot work out that it becomes a challenge.

The court also is self-interested. I do not think the court is going to go out on a limb and expose itself in a way that would lead to political reaction or much criticism. One way of interpreting the Constitution, and the way the court has interpreted it through the broad sweep of the 20th century, is that it is sometimes led but has pretty much consolidated the way Australia was going—the way Australian politics and so on was going—in a very different way from, say, Canada, where the moves have been, in a sense, decentralist.

So I think it is an open question. To interpret the Constitution in a more federal way, the court would have to develop a non-engineer's or a post-engineer's type of constitutional jurisprudence, but it is not beyond the wit of judges—Callinan and Kirby, an unlikely combination—to do that. In one sense, you could say that it does not matter what the court does, the political system will work it out, because there is so much flexibility in the political system. Just because the court opens up an area, it does mean that the Commonwealth has more potential weapons in its armoury. Whether it picks them up and to what extent will depend very much on the politics of the day—where it thinks its advantage is, what it can get away with, what the states will allow it to and so on.

Senator BACK: You made the observation about Sydney centred High Court judges. It has been put to us by other witnesses that there ought perhaps be some recognition of representation across the geography of Australia in the composition of the High Court. Would you comment on that?

Prof. Galligan: There is a Western Australian Chief Justice and there is a Queensland Justice and immediate past Chief Justice. In Canada, as you know, they have much more of a regional formula, including one for Quebec judges for civil law. We have consultation. The Commonwealth has to consult. I think that consultation legislation arrangement came out of a previous wave of discontent that all the judges seemed to be coming from Sydney and a few from Melbourne. Again, I think that can be done through legislation. I would not want to put something like that in the Constitution. Whether a Commonwealth government would want to tie its hands to that extent would depend very much on whether the political current was in favour of that. Presumably, if Western Australia and Queensland continue to be strong and get stronger, the ability of Commonwealth cabinets and prime ministers to ignore them—and they are not ignoring them currently—will become less and less. I think these things will happen through the political process.

Senator BACK:..I just go to your comments on competitive federalism. It is competitive between who and whom? Do you mean between states, between states and territories, between the states and the Commonwealth government—

Prof. Galligan: Every which way—and I am sorry Senator Ryan is not here because I think he is keen on competitive federalism. In Australia, and again it is interesting, there is not much talk except by economists and a few others about competitive federalism. All the talk is about cooperative federalism, which is assumed to be a good thing, but, of course, cooperation can be good or bad. Thieves can cooperate, as can businessmen. Look at Adam Smith—you never get businessmen meeting together unless it is to defraud the public, and that sort of thing. Cooperation can be good or bad and competition can be good or bad. Usually, in many areas you have elements of both, and it changes from time to time. To try to get everything cooperative would be silly. We would not try and do that in sporting or most other arenas of life. Also, it is not as if it is going to work anyway. It is very healthy to have horizontal competition among the states, and you do not need people to change states, but it happens through benchmarking. If you are in Western Australia and you see that Victoria has a superior system of higher education, you are pretty quickly going to be putting pressure on the teacher administrators and so on. That will sort it out.

But also—and this is where the politics comes in—there is a good deal of political competition between the Commonwealth and the states. Again, some of that is good and some of that is not so good. That is why, in a sense, I favour a very flexible Constitution. If the states are not doing their job properly, then the Commonwealth can come in. The problem with that is that the Commonwealth, if it has too much money—more money than sense—will tend to come in more than it should. That competition between the two can be bad, but, as I say, if it is well managed it can be good and it can be very productive.

Senator BACK: And you think the COAG process in a perfect world is the process that would sort that balance out between cooperation and competition?

Prof. Galligan: I do not think it will sort the balance out, but I think it will better enable the Commonwealth and states to focus on areas they do have to work out—for example, a national electricity grid or a carbon trading scheme, or something like that, where you do need to work closely together even though there will still probably be quite a lot of competition, within limits, within that. But then outside of COAG there presumably will be other major areas of competition as well. I think to try to put everything in a cooperative or a COAG basket is really much too limiting. There will be certain things you would put there—things that, in a sense, you are in a position with sufficient agreement to work through and work out. Other things you will not be able to and they will remain out there.

Senator BACK: Relevant to this discussion, this morning the Australian Local Government Association was a witness before the committee pleading the case for constitutional recognition of local government. In the context of this globalism, localism, constitutional adequacy or otherwise, would you care to comment on what you believe would be the impacts, both positive and negative. The CEO of the association was at some pains to say that all they really want is recognition in the Constitution so that it can guarantee federal funding but not in any way interfere with the integrity of the relationship that local government has with the states under their constitutions.

Prof. Galligan: That is perhaps not a dishonest but an inadequate answer or position because, of course, if you get constitutional recognition in order to bolster your independence and your direct relationships with Canberra, that is going to impact—it is the other side of the coin—on the states being the primary or sovereign controllers of local governments. My own view is that local government is important and increasingly important. It is being required to cover a whole new spectrum of social policy issues.

Senator BACK: In the services areas, yes.

Prof. Galligan: Yes, and it is underfunded for the most part. But I think that ought to be handled within the state. I think they should be recognised in state constitutions, if that is where you want to recognise them. I do not see a good case for putting local government in the federal constitution. I think that, in a sense, they are trying to get in there to get some leverage and distance from the state governments, and so state governments would oppose it. The record for constitutional changes is that repeats do not get up—this has been tried before. If it were put again I am pretty sure it would not get up, but, as I say, I do not see a good reason for putting it up. It seems to me that the Commonwealth can give them money and all sorts of things currently—and it is—without changing the Constitution and giving them a guernsey there.

Senator BACK: There seems to be a lot of tension in relation to this allocation of funds from the Commonwealth, be it to the states or local government. You made the observation in relation to the Northern Territory that, once GST funds are passed over to them, they can do what they like with them. I was not aware until coming through this process that, once funds are allocated from the Commonwealth to whatever instrumentality or agency is going to expend them, the Auditor-General does not have the capacity or the right to follow the money trail through to its expenditure. Do you believe that is an appropriate process or do you think we would be better served in a process whereby the Auditor-General did have the capacity to be satisfied and ultimately satisfy the taxpayer that funds that are tied for an expenditure are used for that purpose and are used efficiently?

Prof. Galligan: I used to be an auditor. That is attractive in the sense that, if somebody is giving money, they want to know that it is used for the purpose for which they gave it. On the other hand, if you allowed the Commonwealth Auditor-General to audit the trail right through to the final expenditure point then really there is no point in having a grant; you may as well have it as a Commonwealth expenditure almost because the Commonwealth has the responsibility right through its instrumentality to make sure it is spent according to the Commonwealth's ways. That might make the Commonwealth happy, but I think that would be a pretty severe dint on federal independence that I do not think I would support.

Clearly, the Commonwealth can specify things if it is a tied grant—and increasingly it is doing this, but on the other hand it has broadbanded things because for other reasons it does not want to specify too narrowly and have myriad programs. They can specify basically what they want. There has always been a problem then of how you get a strong state government like Western Australia to do what you tell them to do with the education money or with some of the money. I think part of that is better intergovernmental agreements and management from the Commonwealth's side. The Commonwealth does have the stick. If it knows pretty well that the money is not being spent even if it is not audited then it can use other means to try to bring the states to heel, but the states have an interest in not being too closely tied to the Commonwealth. They certainly would not accept the Commonwealth Auditor-General going to their local schools or wherever the money is being spent. I guess the short of it is that I would not support the Auditor-General going that far.

CHAIR: On the point of constitutional recognition of local government: your proposition is that no compelling case has been made as to why it should occur. I guess the converse is: do you see risks and dangers were it to take place?

Prof. Galligan: It is a bit of a fudge I think. It is not that I do not see a good case; I am not in favour of it. Senator Back mentioned the spokesman saying they wanted that in order to be able to get more readily Commonwealth money but in a sense they do not say that and that would not be what would be put up. It would be simply: 'We want to be recognised in a sense for what we are. We are significant, so mention us in the Constitution, like recognising Indigenous people.' I think that would be the way if it were going to be proposed it would be done—'Local government is an important part of Australian government' or something like that. That on the face of it would be pretty innocuous. The purpose of local government is really more than that. It is to try to get out from underneath the state governments, act more independently and get more money directly from the Commonwealth. Depending on the Commonwealth, it might from time to time see that that is a good way to go, particularly if it has these problems in dealing with the states.

CHAIR: I think Senator Ryan put this point quite eloquently this morning in relation to the local government witness. His proposition was: 'We want something like a section 96 power in the Constitution in relation to local government.'

Prof. Galligan: Yes, so that is fairly specific.

CHAIR: Something of that order; we did not discuss the text or anything like that. But Senator Ryan's proposition was that, once you do that, you invite the Commonwealth to provide funds to local government which could actually be subversive of local government in ways which they had not anticipated. In other words, yes, they can provide grants constitutionally, and the problem of Pape would be overcome—if indeed there is one—but the risk that local government is exposed to is that an expansive Commonwealth could start making demands on local government, and perhaps indeed states, which would be inconsistent with the expectations that local government had when they asked for this constitutional change in the first place. In other words, they think it is a bounty and a good; in fact it turns out to be anything but that. Is that a constitutional risk, do you think?

Prof. Galligan: It is similar to the section 96 scenario with the states. On the one hand, the states want this money for the most part, because there are very few programs that they do not want, except that then, through the equalisation system—this is in a sense the qualifier—they get the money anyway. If they do not get it by a special grant, they get it through equalisations, so they are pretty relaxed. Then you say, 'What's the point of this?' It is a sort of political game. For local government, I think, it would be a similar sort of thing. Very few local governments would not want Commonwealth grants to do this, that and 101 other things, particularly in the broader social policy area, but then they would be required to do what the Commonwealth wanted them to do. I think that is part and parcel of it. The point I would make is not so much that they might be asked to do things that they would not want to do. I would not be in favour of freeing local government up to be playing this third-party game between the Commonwealth and the states. I think there is enough of that in the federal system between the states and the Commonwealth, where, although the Commonwealth has the whip hand, the states are relatively strong. In this other scenario, the local governments compared with the Commonwealth are totally weak, so in a sense they would be very much the tentacles, almost—the doers of the Commonwealth's bidding.

CHAIR: In your brief paper on page 2 you make a point about the case for reducing excessive VFI.

Prof. Galligan: Yes.

CHAIR: You further make the point that states and territories would be more financially responsible if they had to raise more of the money they spend, which I have to say is a proposition that appeals to me; it is the idea of being responsible for the money you raise, obviously, rather than spending someone else's largesse. The question then is: what opportunities do you see for states to have that capacity to be able to raise the significant amounts of money that they are going to need to address the kinds of demands and responsibilities that they have?

Prof. Galligan: This is a key area. This really is the elephant; it is a huge area that overshadows most of Australian federalism and most of the politics of Australian federalism—the acute vertical fiscal imbalance. The states, although they complain about this, of course have been complicit in it. The most notable example was Joh Bjelke-Petersen, Queensland Premier, who used to say, 'The only good tax is a Commonwealth tax.' There are the pluses and minuses. Joh preferred to play grantsmanship in getting grants from Canberra rather than levying the taxes himself, with the opprobrium or political distaste that that might entail. For any sort of realignment to come about, the Commonwealth essentially has to lead, so it would be a self-denying ordinance to extend from the Commonwealth, but that is not impossible. Malcolm Fraser, you remember, introduced an arrangement whereby, within limits, the states could vary tax by way of a rebate or an extra certain amount of a few per cent. None of

the states moved on it, for the Bjelke-Petersen sort of reason, and Paul Keating took that out. It would require the Commonwealth, in a hardheaded way, to work-out—and it is not hard to do—the proportion of money they need for all of their purposes, plus all of the equalisation. It would be much less, of course, than what they have currently, and they would have to agree to pass some of that back to the states.

In the Canadian system, for example—and you can still have a coordinated national tax-gathering system, although Quebec is separate in Canada—you have a Commonwealth tax of perhaps 60 per cent. The income tax is Commonwealth and the states bear the 40 per cent. You could have all sorts of rules about how much and whatever, but for that to come about there has to be a political change of mind, particularly at the Commonwealth level but also at the state level. They have to want this.

CHAIR: We are talking about a significant amount of revenue, which you cannot raise from conveyancing fees, land taxes, payroll taxes and things of that kind. The revenue raising that is left to states is inadequate for the purposes we are talking about.

Prof. Galligan: It is the bits and pieces. Originally, the states levied income tax and then the Commonwealth came in, in part, in the First World War to finance that and then took a monopoly in the Second World War, and it has kept it. In most other federations—in fact, I think there are no other federations like this—the Commonwealth raises all of the income tax and all of the indirect goods and services tax. Howard allocated all of the GST back to the states, but you can see that that is a bit fraught, because Kevin Rudd, despite his cooperative federalism boasts, was going to take a third of it back for another share of public hospitals, which I thought was unconscionable. Somehow it did not seem to raise any feathers in the Canberra establishment—senior politicians, bureaucrats, journalists and whatever. They just thought it was fine. So it would be essentially that—dealing the states back. It is in the act that it cannot be changed without total agreement, and Western Australia did not agree. The GST is allocated back, in a distributional way, to the states. It would be a matter of allocating a proportion of the income tax in that way as well.

CHAIR: Part of your submission seems to make the point that the management of the Federation is under-institutionalised in a way—that, compared to Canada, for example, we do not have enough intergovernmental contacts. They exist through COAG and they have existed through other mechanisms in the past. The kind of structure that you need to manage a sophisticated 21st century federation is, essentially, not in place. We do this in a very incomplete way, but we also do it in an ad hoc way. The proposition was put to us in an earlier hearing that the Commonwealth is managed in, essentially, a crisis management way. Every so often we realise that there is a problem and we try to solve that problem rather than having a kind of continual review of the Federation in some fashion. Is that a view that you share?

Prof. Galligan: It is not just crisis management; there is an enormous amount of public attention, media attention, intergovernmental management and so on below the surface. There are officers throughout the major departments in the states, including in the premier's department, who spend much of their time liaising with colleagues almost on a daily basis—even more than that—in Canberra and the states. So there are a whole lot of ongoing things that are not crises and can be managed, in a sense, in that way, but it is in a rather informal way. It is like this: 'I'm the director of some aspect of education and I know you as the Commonwealth one. I can call you at any time and we can work things out.' A lot of things are solved in that way. When things become crises, political leaders get involved and you often have stand-offs and so on. Broadly, I agree with the way you were putting it—that it is rather ad hoc, whether it is this ongoing administrative issue or a crisis, and COAG is cranked up or cranked down according to the propensities and political interests of the current Prime Minister particularly. The states do have their own meeting, but that is pretty ad hoc again and informal. So I would think broadly, yes, we do need, and you would expect we would have, a more sophisticated institutional platform for intergovernmental relations. In other areas, like equalisation, we have a very elaborate institutional organisation to support this, but in mainstream intergovernmental relations we do not.

Senator BACK: It has been most interesting. Thank you.

CHAIR: Professor Galligan, thank you very much for giving us a submission and thank you for your time today. We very much appreciate you coming before the committee. It has been most helpful.

Prof. Galligan: Thank you for listening and inviting me in the first place. Good luck with your recommendations.

UHR, Professor John, Private capacity

[14:41]

CHAIR: Thank you very much, Professor Uhr, for attending the hearing today. We very much appreciate it. We received a letter from you dated 28 April. We are just debating as to whether or not we should regard it as a submission to the committee or whether or not we might regard it as additional information. Perhaps the latter would be an easier category. Are you content for us to regard it as additional information to the committee?

Prof. Uhr: Make whatever decision you think is appropriate.

CHAIR: If you would care to make an opening statement, we would be happy to hear it. Then we will ask you some questions. If not, we can move straight to questions.

Prof. Uhr: Just as background to the three propositions I put in the letter let me just observe one or two things. One is that federalism as a concept is just so hard for any of us to get our heads around. It is really very difficult. It is difficult to understand because it is about dispersing power, and most of us are much more attracted to concepts and institutions that bring power together. We can understand them better. I would not be surprised if you are finding this difficult, because all of us have difficulty with the core concept that lies behind the institutions of Australian federalism.

Practices of federalism vary enormously. The concept is difficult and then the practices vary enormously. There is no one model of how to do federalism, and the Australian model is similar in some ways to other countries and different in many ways. Australia is unique because of the institution that you represent—the Australian Senate. There is nothing like it at all anywhere, so that stamps a unique character on Australian federalism. There are lots of other parts that Brian Galligan has just been identifying that show that we overlap in some ways and have shared tendencies with other federations, but we play the game differently.

As a result, most people really do not understand it. Most Australians do not understand federalism. It is too hard. Most of my university students are deeply ignorant about it because people like me do not teach it. The Australian academic community is kind of shy about federalism because it is so complicated to unpack and explain. Many of my academic colleagues are suspicious of federalism because it seems to be antidemocratic in some ways; it is sharing things around. They would prefer a majoritarian model of concentrated power with strong leadership where you know who is in charge and who is responsible if things go wrong.

Given all those things, you have a wonderful opportunity to help contribute to better public understanding if you can gather together some mechanism or process to identify some champion. Once you finish your work and go back to the many other things that you have to do and this committee is dissolved, if you can leave behind something that can act as a lighthouse or a beacon for better public understanding of federalism in general and the state of the Australian Federation I will be your champion. I put those three propositions in a letter to try to identify some of the things that I think you could recommend that could remain in place once you have gone on to do other work.

CHAIR: Thank you very much. On this theme that you have been elaborating upon, I suppose, I am seeking an explanation because you are the former head of the ANU's Federalism Research Centre, which is one of the few federal research centres we have had anywhere—I think I am right in saying that—in any academic institution. I am interested to know why that no longer exists. What happened to the funding et cetera?

Prof. Uhr: You will have to call back the former witness, Professor Galligan.

CHAIR: I should have asked him that.

Prof. Uhr: He was the penultimate head. I was the undertaker who came in at the end.

Senator BACK: What did you do wrong, the two of you?

Prof. Uhr: Brian was there when the decisions were made and it was my melancholy duty—

CHAIR: We hold you both culpable, do we?

Prof. Uhr: No. It was a decision by both the Commonwealth and the state that after 23 years enough was enough. These were committed public funds that had served a very important public purpose. The states had matured remarkably. The states had got closer and closer to the Federalism Research Centre, which was initially funded just by the Commonwealth. The Commonwealth was getting a bit shy about that. The Commonwealth was the pacesetter that put the money in initially to provide a scorecard as to what was happening. I think that at the end of 23 years it had probably served as much public usefulness as it was likely to serve at that point and there was an expectation—unfulfilled, I suppose—that the states would establish a state specific centre, not necessarily

in Canberra but somewhere, that could act as a gatekeeper for the states, a bottom-up version of the Federalism Research Centre.

CHAIR: Is it your view that there is a need for something similar, if not an institution with precisely the same mandate then at least an institution which looks at this? I know you have made a point in relation to the Senate's role here, and I will get to that in a moment. I am thinking about an institution which has responsibility for the academic study of federalism, and that seems not to exist in the country at the moment.

Prof. Uhr: Yes, it seems not to exist. The political science community is pretty small. They are the ones who acted as the custodians of it in the past—political scientists and economists. There is no one centre now. That would not necessarily be a bad thing if there were a range of centres and people could pick and choose. That has not happened. Why that has not happened I am not sure. It is a hard ask, because you are inviting governments to put money into public institutions and ask them to call it as they see it. Governments are cautious about that. They might look to universities to help refine and deliver policy or to help with program implementation, but to ask universities to stand back and blow a whistle from time to time when they think something called federalism is not being played according to the spirit of the game? I can understand why they might be cautious.

CHAIR: I think we all understand that too, as members of the federal parliament. But I suppose there are ways in which you could do it through centres of excellence and things of that kind. One of the options open to the committee clearly is to make a recommendation which involves providing funds for the creation of a centre which we believe would be of continuing value to the Federation. I am interested to know whether or not you can see some value in that.

Prof. Uhr: Sure. You can see how that practice works with medical research and the Australian Research Council. They have a designated charter of priorities. That charter changes from time to time. It reflects the advice they give to government and the advice they receive from government. So it is not impossible for body like the Australian Research Council to take note of the importance of federalism over the next three to 10 years or something like that and just see what happens. As it happens, I know that there are academics who have put in proposals on federalism and been successful, so it is not as though it is not featuring now. But it could easily be slotted in as a kind of national theme. If it does not work out, they can unslot it. It happens, as I say, with medical research as well as the Australian Research Council. Once you make a recommendation that they give consideration to that, you are also asking government to supplement the funds of that organisation. That is more than welcome.

CHAIR: I do not think we have had an academic before us who has not made that point. But your suggestion or your proposition in relation to the Senate is of a different character, as I understand it. It is not so much to undertake academic research; it is to focus the parliament's attention on the continuing issues of federalism. Is that a fair summary?

Prof. Uhr: To focus parliament's attention but more particularly the public's attention. It would be to provide a mechanism by which public attention is drawn to federalism by having a dedicated Senate committee from time to time take an audit of what is happening in Australian federalism, hold a watching brief on COAG and then engage in this regional Asia-Pacific dialogue with similar bodies that are looking at similar variations of federalism, which are just wonderfully constructive in ways that we can contribute to but also learn from. Public understanding is the test that I would provide for the success of any of these mechanisms.

CHAIR: Are there examples of that kind of structure in other federations of which you are aware?

Prof. Uhr: Not really. In the Australian Federation, Brian will know more. The Victorian parliament established a committee on Federation back in the nineties which is no longer in existence. The Western Australian parliament at one stage, I think around the same time, had a committee looking at uniform national legislation and the effects that was having on the state of the Federation. These things come and go. There is nothing that I know of at the moment. In Canada there are policy specific inquiries rather than a generic capacity to keep a check on what is happening in developments in federalism.

CHAIR: The challenge, I suppose, is to work out a mandate for that kind of committee and determine precisely what its responsibility should be. You mentioned COAG, for example. I can see the point about the committee having what would be perhaps—please correct me if I am misunderstanding your point—a parliamentary oversight of COAG's general activities. Is that part of the intention?

Prof. Uhr: That is correct.

CHAIR: The question is: how wide do you draw the mandate for a committee of this kind?

Prof. Uhr: I think COAG is exactly the place to begin because you are looking at the holders of executive power across the country that are exercising that power in the name of the Federation through COAG. No one

parliament is really in a position to monitor the institution of COAG as a whole. I do not think any other parliament is trying to do it in relation to their own team of ministers.

The Senate, by definition, is a federal body. We really should see it as part of the institutional logic of having a Senate that it does something specifically in the name of the Federation. If it is a committee that only has one inquiry per year and that one inquiry is a status report on what is happening in COAG, that would be wonderful. I do not think it needs to be, like many other Senate committees, overburdened with inquiries and references all of the time. It is something that is there keeping an eye on COAG. It would certainly provide an opportunity for state officials in particular to air some issues they think people in Canberra might not fully understand, and that would be wonderful. You will have a chance to explore that this afternoon.

CHAIR: You will be aware of the issue that some parliamentary committees have the capacity to undertake inquiries of their own volition and others are required to take references as a result of government intervention of one kind or another. Do you have a view as to how this committee should operate in that respect?

Prof. Uhr: A brief standing order that allowed the committee to keep an eye on and report periodically on COAG would probably be sufficient. If it then wanted to take references from the Senate on broader issues affecting federalism or other policy aspects, that is a door that should be left open. But I think the initial brief should be one of oversight and accountability for the most remarkable experiment we have had in shared executive power, which is COAG.

CHAIR: But it should have a measure of autonomy. Is that right? It should be able to decide for itself what its brief is and what its agenda should be.

Prof. Uhr: And decide how it looks at COAG. The standing order should allow it, on the basis of its understanding of developments in COAG, to report back to the Senate that it is now opening up an inquiry into some aspect that comes out of its annual report or annual inquiry.

CHAIR: I will go to my colleagues and then I will come back to you later.

Senator MOORE: A number of other people have suggested that we have some kind of independent body looking at the Constitution as opposed to Federation. I think you are the only witness who has talked about having some kind of standing group to look at the whole issue of Federation. A number of academics have said they wanted some form of organisation looking at the Constitution. The two things would not be mutually exclusive, I would think, if there was an organisation that was looking at the role of the Constitution. We asked a couple of them and they said the major point would be to keep it on the agenda. People do not know about the Constitution and they do not understand it. If something around the Constitution was developed it could also have a link with federalism, I would have thought.

Prof. Uhr: Sure. They are not exclusive at all; they overlap. What I was looking to was the national parliament, which has a federal house, taking some small step forward to have a permanent contribution to public understanding of the way we do federalism. The executive governments have stolen a march in the practice of federalism. It is undoubtedly a good thing that they are working together. That is just the tip of an iceberg. You know there are many, many examples of ministerial councils that are operating independently of COAG on heaps of important policy issues. Some Senate committees get involved in monitoring and investigating them. The Finance and Public Administration Committee used to try to report annually on the existence of all those committees. That was difficult enough. So my suggestion is really just for the Senate to carve out a little bit of that space. There are plenty of other opportunities for other expert public bodies to do wonderful contributions to public understanding of other aspects of Australian constitutional practice.

Senator MOORE: I am interested with your recommendation linking to the Asia-Pacific region. What is the background to that?

Prof. Uhr: Teaching and teaching students who are experimenting with versions of decentralisation and devolution in different countries: Indonesia, Thailand, Cambodia, Vietnam and China, in particular. They are all very interested in Australian federalism. They all want to know how we do it. We are a huge country with a small population and somehow we seemed to have managed the regionalism game, at least at the political level. They are intensely curious. They are saddled themselves with interesting experiments that we can partly contribute to but learn from as well. Lots of international donor organisations keep travelling around the world insisting that federalism is a kind of precondition of a responsible, modern democracy. A lot of these countries are just being forced to devolve responsibility down and they want to know, then, how you work the relationships between the region and the centre. Here we have a huge regional example of it that they are curious about, and they have lots of other field experience that we need to know more about. It is a wonderful opportunity, if I were a senator, to

meet with like elected officials in the region and to see what roles they are playing in the devolution, decentralisation processes in their own countries.

Senator MOORE: Thank you.

Senator BACK: I think you have given us three very interesting propositions. I concur with Senator Moore in terms of your first, and that is that, if the committee was minded to make such a recommendation, we should somehow include the reference to the Constitution as well as the federation. It is a very courageous group of senators who might take this to the executive of the day.

With regard to COAG—and I do not want to sound party political here and I attempt not to—but it is of interest to me that had, for example, the Carpenter government continued in Western Australia, we may well have had a situation in which there would have been agreement for a third of GST revenues to be taken back in terms of health. It is not quite in line with the paper you have given to us, but do you see whether that in itself is a risk; and, secondly, in the event that it was and was undesirable, how we could structure COAG differently so that decisions of that type in fact might not be able to be made at a COAG level?

Prof. Uhr: I have two comments, Senator. One, I share the views of the previous witness, Professor Galligan, that just took me totally by surprise. A was outraged that the Prime Minister at the time was able to exercise the kind of moral power and persuasion that he did such that it was really unchallenged—it just seen to be another bit of the political game that is played. That seemed to be really cutting right into the whole small c Constitution of the GST. So anything that can minimise that kind of temptation for a federally based, Canberra based executive government to play those sorts of games should be encouraged.

How could this committee or those of us thinking about the results of this committee help? An annual or periodic appraisal of COAG would at least provide an opportunity not to change the way COAG does its business but for people who have views about how COAG could change its business to come forward and have an official standing somehow close to the centre of government for their views to be heard. At the moment it is really just people reaching for a keyboard and hoping one of the newspapers will take it up—or reaching for a telephone and hoping that a radio will take it up. Having a committee like this able to call into being a body of people with an interest in monitoring COAG I think would be wonderful, because it means then that the committee does not have to do the work of becoming experts on how to improve COAG; you just become the medium by which those views are brought closer to government. That is an indirect way of doing it, I accept that.

Senator BACK: I notice that you gave as an example the Audit Office having some involvement in highlighting which levels of government are accountable for what levels of performance in policy implementation and then presumably in some way commenting on their effectiveness in delivering on those policies.

Prof. Uhr: I heard the exchanges earlier this afternoon.

Senator BACK: That is certainly something that you hear from interested people within the community. I was going to ask you to comment, if you would, on Professor Galligan's reference to cooperative as opposed to competitive federalism. I was most interested in what he had to say there and I think it was very sensible in terms of what is possible and what is idealistic and unlikely. Could you give us the benefit of your thoughts on what role this committee might have? Would its role only be to comment, measure and audit? Or do you think its role might also extend to determining or advising which is the most appropriate level of government to be offering some of these different policy implementations?

Prof. Uhr: I started working in Canberra in the 80s, which is a long time ago. I was working with the Joint Committee on Public Accounts and Audit, which was one of my first jobs in Canberra. One of the first things I learnt was the limitations of the Audit Office, as it then was, and how strenuously the Audit Office was trying to work in partnerships with the state bodies because public money was just so hard to trace. The performance and accountability issues associated with managing the stewards of public money were just so diffuse. I am happy for the committee to exercise anything that it can to encourage Commonwealth and state audit bodies to hang in there and work together.

The suggestion in the letter that I have given you only mentions the Commonwealth audit body because you are looking primarily at Commonwealth funds or Commonwealth sourced funds. I do not know where they are at now with the protocols on partnerships with state bodies but it would require both ends to have the confidence to be able to join things up in such a way that federalism gets a better picture and the accountability is more properly washed through the system. How could a committee like this do that? By giving some courage to the Commonwealth audit office and the state audit offices, in the name of federalism, to work together—that is what I would hope for. I have a minimalist model in mind at the moment which would be for you to recommend a really modest step forward that would allow people to gather around and identify things that need to be done.

The mechanisms that could carry out the improvement probably begin with the Commonwealth audit office—and they will be the first people to tell you that there are limits to their resources and capacity—but they require at some stage a kind of federal audit function to be devised where the Commonwealth and state audit bodies work closely together. It is probably the last thing that COAG would want a witness to be telling you.

Senator BACK: In reality, a lot of this information is probably out there now. Should this body come into existence, part of its role would be to just collate it under one umbrella of information so that it would then be fulfilling the role you speak of—that is, informing the community because at the moment the community may not know where to go to seek—

Prof. Uhr: Most of us do not know where to go. The ancillary function that operation would perform is that it would then provide an invitation through the committee for people managing those funds to come forward and explain either their success or relative failure. That is the missing ingredient at the moment. Establishing where funds are is hazardous enough; establishing why they are not in the right hands at the right time is really the important policy issue that needs to be brought before a committee or members of parliament.

Senator BACK: In a sense I think the point you make, which will not be lost on this committee, is that the Senate is probably the only appropriate body that could actually undertake this role. COAG is not going to report on it.

Prof. Uhr: We have had the centenary of Federation so we have a long track record to look at. There is nothing else yet at the Commonwealth level. There is nothing at the state level, and we have six of them. The two territories would be keen to innovate but they have not done anything yet. So, yes, the ball is before the Senate and maybe before this particular committee at the moment.

Senator MOORE: We also need state support. Certainly, the model of COAG is 'equal partners working together'—which we know falls over from time to time. The Senate is still a federal or national body, so to have the absolute engagement of the states in such a body would be a leap of faith for them as well.

Prof. Uhr: Yes, I guess they would be taking it on trust in the first instance, which is why I can imagine that any committee that was established to monitor COAG would in the first instance have an information-sharing role in order to—

Senator MOORE: Establish trust.

Prof. Uhr: build trust, yes.

CHAIR: I have a couple of questions which go somewhat beyond your submission. One relates to COAG, and we have certainly heard plenty of evidence that there is a view that the institution of COAG needs to be more institutionalised—that it needs to be put on a stronger foundation, that the role of the states needs to be clearer, including their capacity to set agendas in relation to COAG, and that there needs to be a clearer process of reporting. There are a whole series of things that people have suggested to us. Does any of that find favour with you, to your way of thinking? Because all of that is not inconsistent with the proposal you are putting here; it is just another dimension of COAG activities.

Prof. Uhr: That is a very good point, and I heard your discussions with Professor Galligan. I can imagine two ways in which COAG could be institutionalised. One is an inside-out operation where the people in Prime Minister and Cabinet now, who have the primary federal responsibility, redesignate themselves in some ways so that there is a clearly identified core within Canberra managing the process and they have a close public relationship with each of the participating states, and somehow we can all see they are part of a shared organisation of some sort. But I am not waiting for that to happen. There is some advantage in it not happening, because I think it is a very flexible instrument. Its success is that it has been able, particularly since 9-11, to work really quickly to establish shared protocols and shared partnerships. September 11 really changed COAG dramatically. It changed Australian federalism by giving a common focus on security, and shared intelligence and shared information in a way that was resisted before 9-11. So it was a dramatic turning point. Any institutionalisation that slowed down COAG's ability to quickly respond to a world that is changing so dramatically would be a bad thing, so I would not want to lay that on COAG.

However, there is an outside-in form of institutionalisation which this committee or the committee proposed by this committee could contribute to, which is just to identify the people involved—identifying the officers as though they are part of a shared agency or a shared process; they come together. Their names might well change, but their roles do not. If this Senate committee could start to monitor the functions, the roles, that are being performed and identify the relationships between Commonwealth and state officials, that, I think, is the sort of institutionalisation that I would like to see encouraged—that kind of virtual relationship or institution.

CHAIR: My COAG question was on the theme of your remarks, but my second question is not. I wanted to ask you about your views, if you have any that you want to share with us, about the constitutional recognition of local government, which is of course a specific term of reference for the committee and something about which we have heard a great deal.

Prof. Uhr: I guess I am in a similar position to Professor Galligan: happy enough to see it literally written into the Constitution; cautious about seeing local government sit alongside the states as though they were equal partners negotiating and cutting deals with the Commonwealth. The federal spirit seems to be that we have a compact between the states and territories and Canberra. The arrangement with local government is that it is represented by the bodies that are taking their story to Canberra. I am just cautious about seeing anything in the Constitution that suddenly complicates the arrangements at the Canberra end so that there are many, many more institutions turning up to have deals cut.

CHAIR: Yes. Yet there does seem to be some dysfunction here in relation to the distribution of revenues. I think that the Local Government Association, whether or not we find favour with its argument for constitutional recognition, nevertheless makes a fairly compelling case that more and more is being asked of local government and they are not necessarily receiving the revenue that they need to undertake those responsibilities, so cost-shifting is taking place at very significant level. So there does seem to be an issue here which needs some kind of attention. Recognition in the Constitution of itself is not necessarily going to provide that solution, except in so far as it might provide the Commonwealth with the ability, unfettered by the problems that the Constitution now presents—a la Pape, for example—to provide that funding.

Prof. Uhr: One of the issues is to try to identify what the problem is in the eyes of the champions of local government. What is the problem? The way it is often presented is that their status and credibility is invisible and they want that to be redeemed in some way by having the Constitution recognise them. I suspect the real problem is the state governments and the issue of recognition means that somehow they can bypass the state governments or have the Constitution allow them greater leverage with the state governments. I think the problem is really the relationship in each state between state and local governments. The Commonwealth has been a kind of saviour in the past; not a problem but a saviour. It is a probably a complication to state governments that the Commonwealth is there providing lifelines of resources to the local governments. From the local government point of view I imagine the problem is not Canberra or the Constitution; the problem is the state governments. Anything we can do to bring vitality back to the relationship between local and state governments is where the solution lies; the Constitution on its own is not going to provide that answer.

CHAIR: A solution to that problem, insofar as it concerns the Commonwealth, would be to make a special purpose grants, or section 96 grants, to the states specifically for local government. That clearly is a constitutional act which is not subject to question. It would address the problem to some extent.

Senator MOORE: It does not recognise local government in the Constitution.

CHAIR: No, it does not do that. If this is a revenue problem specific to the relationship between local governments and state governments then it might address the problem.

Prof. Uhr: It is not just a revenue problem. Think of the way local governments come and go at the whim of state governments—that is the problem. If you are operating a local government the whole regime can disappear overnight according to schemes by state governments. The issue of constitutional recognition is designed to act as a kind of surrogate for some sort of protection against that kind of power of whimsy in Macquarie Street and other streets.

CHAIR: Part of the solution that has been suggested to us is that it will recognise local government in state constitutions but they are essentially acts of the state parliament and they can be easily changed. That is not a solution, I gather.

Prof. Uhr: Yes.

Senator MOORE: I am really interested in your comment about the flexibility and the change that happened to COAG as a result of 9-11. We did see them move quickly on issues of security, particularly around airports and travel, which was long overdue in terms of the national focus on aviation and so on. However, I am interested to know whether you believe that that kind of focus followed through into other aspects of COAG operations. I am interested because I have not heard that put forward before. We all saw what they did in security but your link with that to a change in the way they operated in other ways I have not heard actually put forward before and I would like to get a little bit more on that.

Prof. Uhr: Two aspects stand out for me. One is that 9-11 and the counterterrorism strategies that were then devised by Commonwealth and state officials acted as a kind of spur and a model for other forms of cooperation

in other areas, so that the models of adept partnerships that rose out of 9-11 were then broadcast across the policy stream into other areas. People then said, 'Well if we can do it in border protection and airports and the other facilities, surely we can do it in other areas of public policy'. It became a kind of pace setter.

The second one was that individuals move around. This is a very small federation compared to some others and there are a small number of officials who keep travelling around state and Commonwealth governments to manage things. Sometimes they are managing national security, sometimes they are managing health and sometimes they are managing other forms of infrastructure, but they are all sharing how to manage things. And 9/11 became the laboratory for how to manage better. People who were in Canberra at some point then moved to the states and then to other states and national security became the biggest kind of employer of new talent. That then had a wash on effect in other areas of intergovernmental management.

Senator MOORE: You have actually seen this at work. I totally accept the dynamic around the antiterrorism stuff, but I am understand trying to see where in another field you have actually seen that same focus lead on or whether it is just an assessment of watching the way they work.

Prof. Uhr: Think of small things—traffic management. Just think of people in uniform. Sometimes they are Army; sometimes they are police. They are managing traffic. They do it for different reasons. September 11 means we have a particular pressing reason—international insecurity—and then that flows into domestic management of how the public roads are kept in an orderly way in times of 'normality'. That is a small example. There is hospital management. We have to have hospitals prepared and ready for a crisis. That is going to have an effect on better management of hospitals full stop, because it forces us to think about what the real priorities are—best use of hospital facilities.

Senator MOORE: And then it flowed on to the Bali stuff and the emergency support in the hospitals.

Prof. Uhr: Sure, lots. Immigration, of course, would be a standout case.

Senator MOORE: Massive. Thank you.

CHAIR: If I may, I have one more question, which I asked Professor Galligan. There is this central problem about states themselves not having enough revenue. I am attracted to the proposition that you should spend only the money that you raise; it seems to me that that is a discipline which ought to recommend itself to government as a proposition. Do you see any means by which the challenge of providing revenue to states to undertake their purposes can be solved other than through some kind of change to the way in which we manage income tax in the country?

Prof. Uhr: Internationally, that is the standout example of allowing subnational systems access to revenue that they can then use on purposes that they determine on their own. We have our own local history that helps explain why our Federation is different: it is really the Second World War and the taxation cases. Every federalism is going to have a different path of development. Somehow that stamped us with a 'trust Canberra' path, which we are still living with. Even the GST is a 'trust Canberra' path. I am really not sure how you would supplement that path in this particular Federation, Australia, in such a way that both the Commonwealth and the states would be comfortable with own-source revenue from the states of a substantial kind. I do not know whether the states have their heart in the income tax option; I suspect not. Even if the Commonwealth wanted it, I suspect the states would still think, 'Better to have the haggles that we now have,' partly because of COAG. It means that they have a regular opportunity to eyeball and get very close to the people who are making the recommendations on what money they get and how they should spend it. It is a very cosy arrangement. There is not a lot of discomfort attached to it. There are headaches, but there is not a lot of discomfort. As I say, just because other federations have a greater reliance on self-sourced income from subnational levels, it is not going to provide a model for us; it is just something else to observe from. As we travel within the Asia-Pacific, we might discover more ingenious ways in which subnational governments can have access to revenue that we are unaware of at the moment because we just fly over them rather than spend time in them.

CHAIR: I cannot imagine that any source of revenue has escaped the attention of any level of government.

Prof. Uhr: There you are, so we have an incentive to go study.

CHAIR: But there may well be such a source. Thank you, Professor Uhr, for coming before the committee.

Prof. Uhr: Thank you to the committee.

Proceedings suspended from 15:18 to 15:34

ENGLISH, Mr Dominic, First Assistant Secretary, Department of the Prime Minister and Cabinet

FITZPATRICK, Ms Mandy, Manager, Commonwealth State Relations Division, The Treasury

PERRY, Mr Ronald Thompson, Assistant Secretary, COAG Unit, Department of the Prime Minister and Cabinet

VROOMBOUT, Ms Sue, General Manager, Commonwealth State Relations Division, The Treasury

CHAIR: Welcome, ladies and gentlemen. Thank you for appearing before the committee this afternoon. We have not received submissions from either the department or portfolio areas. Does anybody wish to make an opening statement?

Mr English: No, we are happy to respond to questions.

CHAIR: I might begin with some of the evidence we received this morning and it relates to Treasury, I suspect. I do not know whether you were watching this morning's evidence from the Commonwealth Grants Commission, but they kind of dumped you in it.

Ms Vroombout: Yes, Ms Fitzpatrick was watching.

CHAIR: Could you to clarify the nature of the review being undertaken of the Commonwealth Grants Commission's responsibilities. I would be grateful if you could also outline the timetable and who is doing it.

Ms Vroombout: The review is being conducted by an independent panel. Former Premiers Brumby and Greiner and Mr Bruce Carter has been appointed to conduct the review. A terms of reference for the review were issued and were part of both the Prime Minister and the Treasurer's press release for the review. They defined the scope of the review. The review is not considering whether we should have horizontal fiscal equalisation, rather it is considering the form of horizontal fiscal equalisation and the terms of reference outline a set of principles that the review panel should have regard to in considering the form of horizontal fiscal equalisation, and they go to efficiency, equity, simplicity of the arrangements, predictability and transparency. They are the key principles. In terms of timing of the review, the review panel is to provide an interim report to the Treasurer in February next year, with a final report in September next year which will then be considered by COAG, with a view to a final decision being taken before the end of 2013.

CHAIR: Will the review decide on its processes or do you anticipate that it will proceed in what might be regarded as the normal way—in other words, it will seek submissions and conduct public hearings and things of that kind?

Ms Vroombout: The first meeting of the review panel is tomorrow and the review panel will be considering those sorts of issues. The terms of reference do talk about the seeking of submissions from the public.

CHAIR: In terms of the support that the review will receive, the secretary of the Commonwealth Grants Commission explained that he anticipated some of his staff would be co-opted to the review—is that correct

Ms Vroombout: A secretariat to support the review panel is being established within Treasury. It will have a number of members from The Treasury itself, a number of secondees from state treasuries and a couple of secondees from the Commonwealth Grants Commission. That is the intention.

CHAIR: Perhaps you could explain the context in which this review arose—in other words, what is the rationale for the review? Why does the government think it is needed and why now?

Ms Vroombout: I think the terms of reference outline the context and background to the review around significant structural changes in the economy. So we have the commodities boom and the rise of China and India. We have demographic change. We have a growing population and we have changes in technology. All of these impact on the states and territories in different ways. They impact differently across the different states and territories. I guess the intention of the review was to have a look at how the arrangements for horizontal fiscal equalisation work in the context of the changing structure of the Australian economy.

CHAIR: So there will continue to be, as you have said, a fiscal equalisation formula of some kind?

Ms Vroombout: Correct.

CHAIR: Do you anticipate that it could be radically different to that which exists now? Or is that something that you do not propose to speculate about?

Ms Vroombout: It is not something that I have a particular view on. I guess that will be a matter for the review panel to consider as part of its deliberations.

Senator MOORE: I am interested in the secondees from the states. I think the whole thing is based on COAG and states being engaged as well as the federal level. At this stage have they agreed on the processes? Will it be states determining who will be their representatives or will it be certain states representing a group of states? Has that kind of detail been worked out yet?

Ms Vroombout: The head of the Commonwealth Treasury wrote to his colleagues at the state and territory treasuries to invite nominations. I guess the states collectively agreed on two nominees to be seconded to the secretariat.

Senator MOORE: Two representing eight?

Ms Vroombout: Yes.

CHAIR: I will just go PM&C for a moment. I am not sure how much you have followed the work of this committee and the evidence that we have received but, just put it in context, we have received quite a lot evidence for the view that there ought to be a greater level of institutionalisation in relation to COAG. From my personal perspective I would just like to get a bit of information about the kind of resources that COAG currently consumes or how you are situated so I can evaluate the virtue of some of those recommendations we have received. Can you just put COAG in context for us from a Commonwealth perspective and from an institutional perspective from within PM&C?

Mr English: The core of what we do to support COAG is the provision of a secretariat service, which is managed by Mr Perry's unit and takes about 10 to 12 people at any given time. It works on a range of issues around supporting meetings, planning for the meetings for the Prime Minister as the chair and coordinating the Commonwealth's contribution to COAG. So at its core there is a relatively small unit that looks after what might otherwise be seen as the sort of activities that would be considered in an independent secretariat, if that is what people have argued for.

My perspective would be that it is a coordination activity across a wide range of areas across the Commonwealth and the states. The network that operates between premiers' and chief ministers' departments and the Prime Minister's department through our central COAG unit is quite significant. Within the Department of the Prime Minister and Cabinet at any given time you may find up to a third of the organisation has activities within its remit that are relevant to COAG. Chairing COAG and bringing that leadership to the Federation is an inherent part of being the Prime Minister and the department supports that through any number of activities. In the social policy reform area, for example, our social policy divisions contribute to both advising the Prime Minister on COAG and working with the states and territories on matters that come forward. On the national security side, likewise, there has been a significant agenda in antiterrorism and harmony type issues going back some time.

In terms of the ability to define something that is a discrete function that relates to COAG that you would have in a different organisation, I guess from my perspective the connections that exist across PM&C to support COAG are substantial and, likewise, extensive through the rest of the Public Service in Canberra. Treasury's leadership on elements of that, particularly on the federal financial relations framework, is substantial as well. We would see leading COAG as a major part of the Prime Minister's job, and that is what the department aims to support.

CHAIR: There are 10 to 12 officers, Mr Perry?

Mr Perry: In my unit, yes, there are 12 people.

CHAIR: Is that a relatively stable number? Has it been consistently that?

Mr English: At the moment it is probably a little higher than you would consider to be the ordinary establishment because we are responding to the review of the heads of Treasury's work on the financial framework process, so we have created some extra capacity. It vacillates around that 10 number, depending on priorities.

Mr Perry: And, historically, on the influence or the importance that successive governments have given to COAG work. For a period during the previous government at one stage probably one person dealt with COAG issues in a coordination sense within a department; then over time it grew to three or four; and now, as Dominic has said, we have got up to 12 people who are performing that role. In our counterparts in the states and territories there might be units of eight to 10 people and within the smaller jurisdictions there may only be four or five

working in the COAG space in a coordination sense, but they work very similarly to what we do: those people coordinate their government's involvement.

CHAIR: Each of the premiers departments, I assume, has a COAG unit of some kind.

Mr Perry: An intergovernmental relations unit.

CHAIR: So an intergovernmental relations unit is code—and I do not mean that subversively in any way—that reflects their commitment to COAG as a process. Is that right?

Mr Perry: Yes.

CHAIR: Did you say somewhere between four and eight officers as part of that process is typical?

Mr Perry: In my experience, yes.

CHAIR: COAG meetings take place on an irregular basis; I think I am right in saying that. Perhaps you could explain to us how or when a COAG meeting actually takes place. What can you tell us about the reasons why a meeting of COAG might be called? They are not set down as regular, are they? They take place at somebody's behest, but not at a set time of the year or, indeed, years.

Mr English: Not unlike a whole swag of committees, the chair, at the end of the day, will determine the timing of a given meeting. The aim we have is to be regular, to allow the business of COAG to be transacted, but there are a range of constraints that require balancing in considering when to have a meeting. For example, when we say that 'late in the year' we are having a COAG meeting we will inevitably try to avoid caretaker periods as a matter of course, we will try to balance parliamentary sitting periods and we will also try to look at when the work that has been commissioned by COAG will be available in a meaningfully prepared shape.

Each time COAG finishes there is usually an expressed intent about when the next meeting will be. In February the meeting concluded with the intent that there would be a mid-2011 meeting that would, amongst other things, take forward the commitments to further work that were given at that meeting around health, mental health, disaster preparedness and the like. At the moment we are working within the department to prepare some advice to the Prime Minister that would show when the best time of the meeting would be, given those factors and what we know about the availability of the states, parliamentary sittings and the like.

CHAIR: Is there a COAG operating manual of some kind or a list of protocols? In whose corporate memory is COAG located?

Mr English: I am very pleased you asked, because we have recently re-issued the COAG protocols, which I am sure we can provide.

CHAIR: Are they on the public record?

Mr English: Certainly they are freely available to the jurisdictions.

CHAIR: That is not what I am thinking about.

Mr English: Certainly we are happy to make them available to the committee. As I say, we have shared them with the jurisdictions relatively recently as an update. I do not think we publish them electronically in a public way. They are rather bureaucratic by their nature. We should be able to make them available to people who are interested. But I do not know that they are necessarily the most exciting of reading, personally.

CHAIR: You would be surprised what turns us on!

Mr English: I very much appreciate your interest—I shall leave my comments at that.

CHAIR: You say you have revised the protocols. I am trying to get a sense of procedure and process here and how institutionalised the COAG process is within the context of the department?

Mr Perry: Previously we had had what we call a set of business rules about how meetings would be called, the sorts of things that might go on the agenda, who could put things on the agenda, how we would then proceed into a meeting, the nature of the process surrounding the development of the communique after the meeting and records of particular matters within the meeting. We had business rules up until the beginning of this year and, as Dominic has indicated, we have just recently put together a whole set of new protocols around the operation of COAG, which the states and territories have agreed to.

CHAIR: What significance should we attach to the difference between business rules and protocols?

Mr Perry: I think the protocols now go to several pages, whereas previously business rules went to one page.

Mr English: What was the trigger for the most recent update though, if I can expand a bit, is that we found that the processes around preparing papers and having clear documentation to support decisions at COAG warranted another look. We were ending up with folders that, frankly, the average human being could not carry

into the room, and that was dissuading ministers and prime ministers and chief ministers from reading the papers in any great detail. They were increasingly reliant on briefs from their departments and offices. So we were of a mind to try to get a clearer, simpler structure for the papers together—the sort of learnings that all governments have gone through in recent years about making cabinet processes work better, and taking those lessons through about getting decision-ready documents prepared for meetings. As we were putting that out we updated the expectations around how the meetings would be prepared for. That was the trigger for revising—

CHAIR: Mr English, your proposition to us is that, to simplify, you have become more bureaucratic?

Mr English: One could characterise it that way.

Senator MOORE: Who actually did that? Who did the work on the protocols?

Mr Perry: PM&C.

Senator MOORE: Did you engage with the states while you were doing it or only after you finished doing it and put it out for comment?

Mr Perry: Someone has to always produce a first draft, whether it is the states or us. On this occasion we took the lead, prepared the first draft and then got comments back from the states.

Senator MOORE: Just as a comment, Chair, I feel really strongly that this stuff should be public. Certainly in the health field, where I do a lot of work, there is genuine interest in the way COAG operates, because so many things that have happened have come out of COAG and we are asked consistently: 'How does it work? Who puts things on the agenda?' We will wait until we see it in case it is written in another language, then we will go from there. As a general principle, the guidelines on how organisation operates I truly believe should be completely transparent.

Mr English: I think their provision is unlikely to warrant any particular concern. Given they have been prepared after consultation with the COAG senior officials group, which is the first ministers and secretaries of first ministers' departments, I would feel obliged to let them know that we were going to provide them to you. We will provide them to you as soon as we can after that.

Senator MOORE: On notice, can we find out whether anyone in the consultation group thought they should be public and whether it was an issue of discussion?

Mr English: The discussion that concluded these protocols was a meeting I was present for of the senior officials group in either January or February in preparation for the last COAG meeting. I do not recall that that issue was raised at that point.

CHAIR: I would be grateful if you would take advice on that because I agree with Senator Moore's position on that. I think it should be made available, and we will make it available on our website.

Mr English: Yes. I anticipate no challenge; it is just protocol for the way we handle these documents with senior officials.

Senator BACK: The Commonwealth Grants Commission representatives this afternoon kindly went through again with us the process by which the recommendation is made to the Treasurer for the division of GST funds to the states and territories. They spoke of the averaging concept et cetera. The question I asked was: in that whole process, where is the motivation for each of the states and territories to actually, in a sense, maximise their revenue and contain their expenditure so that for the overall good nationally the drain on the national purse is reduced or at least minimised? They said it was not their role to actually make that determination. I am just wondering: whose role is it? I ask the question in the background of a statement made by one of the state premiers recently about the fact of another state becoming the nation's national park. The obvious suggestion by that premier was that this other state could perhaps be doing more in terms of its revenue base. The premier felt that it was not. I am not necessarily agreeing or disagreeing with what he said. I am just asking: whose role is it to actually, in a sense, keep the states and territories honest in terms of maximising their revenue and containing their expenditure as it relates to GST funding?

Mr English: We would start with the premise that the ultimate accountability for states and territories for the way they raise their revenue and use that revenue is with their electorates. Not COAG, the Commonwealth or the CGC process can be a substitute for that primary accountability. What we have in the horizontal fiscal equalisation arrangements is, at its basis, an attempt to try to distribute that pot of money, which needs to go from the Commonwealth to the states because of vertical fiscal imbalance, in a way where there is the opportunity for states and territories to deliver equivalent services to equivalent standards. But, at the end of the day, I do not think you could presume that a formula will achieve what is really a role for the electorate.

Ms Vroombout: And the Grants Commission process is intended to be a policy-neutral one that neither encourages nor discourages particular actions from the states and territories. As Mr English has said, it is ultimately a matter for the states and their electorates around what particular policy they choose. The intention of the process is that it is a policy-neutral one that, as I said, neither encourages nor discourages particular activity on the part of the states. The terms of reference for the review of GST provide an opportunity for the issue of whether the Grants Commission process should provide particular incentives or not, so the review provides the opportunity for that issue to be considered.

Mr English: I do want to add marginally to that comment before to say that, notwithstanding the basic framework as I have described it, the Commonwealth has pushed this agenda along as much as any other member of COAG has. It has sought to define through the national agreements process a range of benchmarks for the level of outputs and outcomes that services will achieve for constituents that jurisdictions are then publicly held to account against. The CRC reporting process is designed to give an independent source of information for the electorate to assess whether jurisdictions have upheld the ambitions of those agreements. It is based on electorates holding their jurisdictions to account but, by consensus and by agreement, states and territories and the Commonwealth have defined areas in which they agree that we all need to work together to achieve a certain standard of output and outcome for communities and that there will be transparency around the achievements of that through the reportings of the CRC. So there is a sense of some voluntary acquiescence, if you like, to that framework for accountability around the key service delivery areas of health, education, housing and the like.

Senator BACK: So in a sense you are saying that COAG is the most appropriate forum in the event that one or more premiers feel aggrieved at the activities of their colleague or colleagues. You feel that COAG is the most appropriate venue or medium through which that sort of robust discussion might take place. Is that what you are saying?

Mr English: Certainly the intent we have in supporting COAG is to make sure that nationally important and significant issues jurisdictions need to address would be dealt with there. If it were simply a matter of a few jurisdictions with a debate between themselves, then those jurisdictions no doubt have avenues to pursue that amongst themselves. The states have the counsel of the Australian federation whereby they can similarly pursue issues that do not necessarily involve the Commonwealth. So there is a range of layers, and it would depend on the issue. Certainly, if there were some sense that national economic performance was being held back by decisions in particular areas, subject to the chair's agreement and jurisdictions raising this issue for discussion, there is the opportunity for those things to be pursued.

Senator BACK: I think the secretary of the commission made a very valid point when he said that on the expenditure side benchmarking across state and territory boundaries would form a very useful tool. For example, in the per capita delivery of health services or education services, if one jurisdiction is doing it very well one would expect that the others would be watching closely, learning from them and improving. I think that was a very valid response. It is more towards the revenue and the opportunities for revenue that I was probably directing my question. As I said, the Grants Commission was at some pains to say that it is not their role at all. I can understand that, but it did beg the question of whose role it is. When you speak of the electorate, I can understand that within an individual state or territory the people who make up the electorate would say, 'We're very happy with such and such a circumstance, just so long as we keep getting sufficient funds to live a lifestyle to which we have become very accustomed.' I do not think you can answer the question any further.

Mr Perry: From my experience, particularly on the expenditure side, the state treasuries do have regard to the massive amounts of data that go to the Grants Commission. They are always combing through that data to see whether some jurisdiction is doing something better than them—delivering at a lower cost per unit or whatever. Then they will go and ask the hard questions of their agencies.

Senator BACK: I would certainly expect in a robust economy that that is exactly what we would be seeing. My other question is in a totally unrelated area, but you may be able to assist. We have had representation from the Australian Local Government Association strongly supporting an amendment to the Constitution to recognise local government. My question to you is: how might the current arrangements for funding from the Commonwealth, either through the states to local government or directly to local government, change those relationships in the event of local government successfully lobbying for the Constitution to be amended? For example, I look at the Australian Local Government (Financial Assistance) Act 1995, which speaks of the process by which funding goes from the Commonwealth to the states, who then distribute the funds to local governments in accordance with recommendations of local government commissions, having regard to the seven national principles. Pape obviously came up in these discussions but it is not clear to me why it would be automatically the case that local government would do better in terms of its funding from the Commonwealth in the event of a

change of constitution. Again, I am not asking for an opinion; I am simply asking for what would be the mechanism or the process that local government would understand so that it would enjoy better access to the purse.

Mr English: I have to confess it is not clear to us either, that without a further decision by government to make financial arrangements subsequent to such recognition that it would make a material difference.

Senator BACK: You are not aware of the barrier currently that would be broken down in the event of such a move being made.

Mr English: Taking into account the implications of the Pape decision, the Commonwealth remains able to make grants under its general powers in the Constitution as well as make payments to the states for purposes relevant to their responsibilities, which do include local government currently. So it is not clear that we are wanting for lack of opportunity to pass funds to the councils via one mechanism or the other and without further commitment from the budget and some savings to offset it we are not necessarily in a position where we would be looking to make further contributions.

Senator BACK: At the moment, the answer given to me this morning by the Grants Commission secretary was that the commission does not take into account local government needs per se in determining its recommendations to the Treasurer for the GST carve up each year. Is it the case that the review being undertaken by Brumby, Greiner, Carter, as part of its terms of reference, to have a look at local government financing needs?

Ms Vroombout: That is not part of its terms of reference, so it is focusing on the current arrangements which could address horizontal fiscal equalisation in payments to the states and not local governments.

Senator BACK: Yes, but nothing would prevent local government, presumably, from putting in a submission. Are public submissions going to be invited of the review panel?

Ms Vroombout: The terms of reference make it clear that there will be a public submission process.

Senator BACK: So they could in fact represent their case. Thank you.

CHAIR: On the question of Commonwealth grants to local government, the Commonwealth still makes grants directly to local government of the Roads to Recovery kind, for example, does it not?

Ms Vroombout: Yes.

CHAIR: What view have you taken about the implications of Pape for your capacity to continue to do that?

Mr English: To date the approach we have taken is that current arrangements will continue unless subsequent decisions by the court suggest that a particular activity should not. So at this stage we do not expect that Pape has taken away the ability to make those payments.

CHAIR: Have you sought the Attorney's advice on the subject?

Mr English: That is consistent with the Attorney's advice—that we should continue with current arrangements unless a demonstrated need arises to change them.

CHAIR: Is that advice available publicly?

Mr English: That is probably something we would have to put to government because it was legal advice to the government.

CHAIR: Perhaps you could do that, because we are getting somewhat inconsistent evidence about this matter. There is a view that Pape has created a problem with regard to direct grants to local government and this needs to be addressed in some fashion. I understand that the direct grants continue, which suggests, obviously, that you have formed a view that it is not illegal or not unconstitutional to do that. But I would be interested to know the basis upon which you have made that decision. I presume you have an interpretation of Pape but particularly why—

Mr English: Government gave Pape serious consideration but it was determined that that did not need to extend it to a revocation of any particular program at this point in time.

CHAIR: Mr English, have you formed a view that you can continue to do that, or whether you need to be more cautious about the way in which you make grants to local government as a consequence of Pape, or do you think that the area is untrammelled constitutionally so that if someone presented you with a proposition to send money directly to local government in relation to housing or aged care or something of that kind you could do that, or have you not taken those considerations into account?

Mr English: We have formed the view that on payments to other jurisdictions that we need to be mindful at all times about the constitutional basis on which we would be pursuing that payment—state, local government or not. In some cases the payments will proceed under the Commonwealth's ability to make payments to, say,

territories. In some cases it will be on our general capacity to make grants off the Commonwealth's own authority, and to my knowledge we have not especially isolated payments to local government in that process. We have not felt the need to particularly isolate local government in that discussion.

CHAIR: So you have not discontinued a process of grant as a result of Pape in relation to that, okay.

Mr English: No.

Mr Perry: But as Dominic said, we went through a very extensive review in the light of Pape of all of our payments to make sure that we could justify them constitutionally.

CHAIR: I see. I do not think that Pape raised it. In fact it is inconceivable that he could given section 96 of the Constitution and the right to make grants to the states for particular purposes et cetera. Just in relation to that course, what if any expectations does the Commonwealth have about money directed to local government via the states to the extent to which states extract some kind of cost for their administration of a grant? Or are we safe in assuming that any time you give a Commonwealth grant via 96 then all the money that is appropriated for that particular purpose will end up in the hands of the local government?

Ms Vroombout: I think that generally speaking I would say yes, unless the states negotiate as part of the particular arrangement for administration costs to be covered. But if the arrangement does not provide for that, then we would expect that the full amount of the funds as part of the arrangements would flow to local government.

CHAIR: Is it a typical practice for states to negotiate some administrative cost in relation to their administration of those funds?

Ms Vroombout: Not that I am aware of, no.

Mr English: In the simple passing of funds there seems to be little cause for an arrangement that would divert resources to the states and territories. It is a bit different, for example, from the situation for the construction of capital around schools where we did have a particular agreement around a small amount which would be committed to project management and the rest was to be used for the actual construction costs. In those circumstances, you would seek an agreement, but the simple funding of funds is still a procedure—

CHAIR: I do not want to raise the whole debate about BER and so on except in so far as the administrative cost is the same across the Commonwealth. I assume it is. In relation to that, for example, could states negotiate different kinds of management costs with the Commonwealth under the BER?

Mr English: I would have to go back and check my facts on that. Whether the rate was the same across jurisdictions, I cannot recall.

CHAIR: There is a constitutional provision of course against differential grants to states. I am wondering whether it applies to these kinds of management fees et cetera.

Mr English: I should take that on notice.

CHAIR: Would you do that, Mr English? I suppose the question is: have states negotiated different management fees in relation to BER and on what basis have they actually done that? Do I take it from your remarks here that you do not see any impediment if you are passing funds to local government for any particular purpose for the Commonwealth to say: 'Here is the funding. We will pass it through the states and the total quantum of it is to go to local government. We are not permitting any kind of administrative costs'—or whatever the phrase might be—

Senator BACK: Leakage.

CHAIR: Are you confident about the capacity to be able to send money directly via the states to local government and they will get all that has been allocated?

Mr English: Yes.

Ms Vroombout: Yes.

Mr English: It would require a specific agreement for that—

CHAIR: Does the Commonwealth see any advantage in sending it directly as a grant as distinct from sending it via the states?

Mr English: We have payment arrangements that contemplate any number of circumstances. Some of those are designed to be consistent with our constitutional powers. To be fair, these days it would be difficult to make a strong case in either direction based on the practicalities of the payments—

CHAIR: Then do you have any kinds of principles or guidelines as to when you might decide to allocate funding to local government directly such as the Roads to Recovery program or send that money via the states to ultimately end up in the hands of local government?

Mr English: No, I think it would be more of a case by case decision-making process than—

CHAIR: So you do not have preferred processes in relation to areas of Commonwealth or state activity or in relation to particular circumstances that might arise? It is a case-by-case basis?

Mr English: Certainly under the federal financial relations intergovernmental agreement we have agreed that all payments to a state or territory would be provided under those arrangements by treasuries in a single payment that would then be disbursed with the jurisdiction by the Treasury. So national partnerships and SPPs get provided that way. Beyond that, if we were doing a program aimed at meeting a need in local government, we would consider on a case-by-case basis the most effective way of disbursing the funds that recognised either the fact that this was generalised support and could join a generalised support stream or that it was targeted at particular needs like Black Spot funding, which would be more targeted and therefore disbursed in a slightly less bulk way, if you like. It is a payment to the states for the purpose of them to pass on to local government to support their activities as in effect a state government instrumentality then that would bring it under the FFR agreement. That would be my expectation.

Ms Vroombout: That is right.

Mr English: And it would be fed through Treasury.

CHAIR: With what consequence if you bring it under federal financial relations? What follows from that? If you put it in that particular box, what does that mean for the grant?

Ms Vroombout: I guess the key thing it means for the particular grant is that it is a payment from the Commonwealth Treasury to the state's Treasury and then, if it is to be paid to local government, it is from the state Treasury to local government. If it is a payment direct to local government, it would go from the relevant Commonwealth portfolio agency to the relevant local government in the jurisdiction.

CHAIR: I see. So it is an appropriation for a particular portfolio—is that right—

Ms Vroombout: Yes.

CHAIR: as distinct from coming out of Commonwealth general Treasury revenue?

Ms Vroombout: Yes, generally speaking.

Mr Perry: To elaborate on what Sue was saying, if it is under a national partnership agreement, the Commonwealth agency has administrative responsibility for the payment, but the payment is actually made by the Treasury.

CHAIR: Mr Perry, does administrative responsibility mean that the Commonwealth has a capacity to audit that particular grant? Is there an audit trail following either means of doing business?

Mr English: The audit implications are no different under either model. The Commonwealth Auditor-General's role extends to the audit of the use of funds within the Commonwealth. So, once either the Treasury pays it to a state Treasury or the department of transport pays it to a particular council, it means it has left the Commonwealth and it is no longer within the purview of the audit function of the Commonwealth. Therefore it comes under the ordinary arrangements that apply in that jurisdiction. I believe, for most local governments, they are audited by state auditor-generals.

CHAIR: Since it is Commonwealth money to start with, has the Treasury looked at the question of following the audit trail beyond the point at which it arrives in the hands of another level of government? In other words, have you ever given consideration to, or recently given consideration to, the possibility that the Commonwealth's audit powers might extend beyond the point at which it extends now?

Ms Vroombout: There have been a number of suggestions that the Commonwealth Auditor-General's powers should extend beyond their current purview. The joint committee on public accounts has made a recommendation to that effect. Both we and PM&C have been considering that recommendation.

Mr English: Which I think remains without a response from government to date. At the moment the situation remains as it is.

CHAIR: I am not on that committee and I do not—

Senator BACK: I chair the references committee. That is a recommendation—

CHAIR: I think we are talking about the joint public accounts committee. How long ago was that reference made?

Mr English: At the beginning of this year—in January 2011. The report was finished in the last parliament and then released at the first opportunity under the new parliament.

CHAIR: Even I would not be too hopeful about getting an answer in that period of time.

Mr English: That is fortunate because we do not have an answer at this time.

Senator MOORE: Just in terms of the audit process, the recommendation—this is my understanding from the joint public accounts committee—was that it was looking at federal grants and the ability to audit federal money, and that came out of a number of different things. Any decision, though, in terms of extending the federal auditor's powers to follow that money would necessarily, I would think, have to engage negotiations with states.

Mr English: Absolutely.

Senator MOORE: So I would think the ability to say yay nor nay to such a recommendation would need to have a process back through the states and the COAG model to come up with an agreement. Would that be correct?

Mr English: Absolutely.

Senator MOORE: That was following on from the next step, to double-check.

Ms Vroombout: To avoid a double audit—yes.

Senator MOORE: That is right. Extending the ability of the federal auditor to follow the money trail, which is fair, would mean that they would have to have some agreement with their state or territory counterpart, to go into the expenditure in that area. I just wanted to get that clear in my mind.

Mr English: You have that entirely correct, as I understand it.

Senator MOORE: All these details we are talking about—giving grants, how they would operate, the links between grants and them then going onto local government—are they all covered in the Intergovernmental Agreement on Federal Financial Relations? I have not read this document and I do not think that I will. To begin with, I am not sure I would understand it. But I would have thought that the Intergovernmental Agreement on Federal Financial Relations, which is the blueprint, I would have thought, would have had clauses in it that covered the kinds of questions that Senator Trood was asking. Is that not true?

Ms Vroombout: No. The agreement covers payments to and through the states, but it does not cover payments directly to local governments. It is confined to the Commonwealth's relationship from a financial perspective directly with the states.

Senator MOORE: Would there be a paragraph in that document that looked at issues of the transference—the responsibility of the state to transfer money onto local governments, NGOs or any other bodies? Somewhere in the current agreement would we find that it says, 'If a grant is going to the states for the purposes of transferring onto anyone, this is how it should work?'

Ms Vroombout: There is a clause. My recollection is that it says if a payment is made to a state to pass on to somebody else then they must do so as soon as reasonably practical. But that is as far as the clause goes.

Senator MOORE: It does not go into any of the particulars we talked about in terms of needing to negotiate admin fees?

Ms Vroombout: No.

Senator MOORE: So there is none of that. It just says that it is a timeliness issue.

Ms Vroombout: Yes.

Senator MOORE: I know timeliness in the past has been a major concern where money gets transferred but does not get transferred on for a long period of time.

Ms Vroombout: Yes. Then any of those other things that we have spoken about would be covered off in the agreement for the particular payment. So if you wanted particular rules to apply in respect of a particular payment then you could handle that in the agreement for that payment.

Senator MOORE: And that could cover national agreements or any of the national partnerships?

Mr Perry: No. It would be covering national partnerships principally.

CHAIR: It would be covered in the particular national partnership in relation to that area of activity?

Mr Perry: Yes.

Ms Vroombout: Yes, it would be covered in that particular national partnership.

CHAIR: Do they follow a formula or are they essentially negotiated for every particular partnership? Is there a standard?

Ms Vroombout: There is a standard template that is used for them. Each of them, depending on the particular subject matter, will look and feel slightly different, but there is a standard template that is to be used for the negotiation of them.

CHAIR: Can you tell me whether the standard template is one that has been created for the purposes of these partnerships, which are relatively new, or whether it is based on other mechanisms which have been longstanding for passing money from the Commonwealth to the states? Have we reinvented the wheel here? Have we done something innovative, creative and new or have we basically taken something that we have been using for decades and said, 'We will rebrand it'?

Mr Perry: No.

CHAIR: That is not a criticism; I just want to understand the extent to which we have really thought through this whole process by which we pass on funds from the Commonwealth to the states.

Ms Vroombout: I would say that we have created something new. The federal financial relations framework that commenced at the beginning of 2009 is quite new and different in the way that it makes payments between the Commonwealth and the states, and national partnership agreements are a new form of agreement intended to be less prescriptive and focused on outcomes rather than input controls. The template has been designed in the context of the new federal financial relations framework rather than the quite detailed funding deeds that existed prior to that framework commencing.

Mr Perry: It is quite a deliberate process—

CHAIR: Mr Perry, you look like you are itching to say something.

Mr Perry: No, I was just agreeing with Sue. In the early days, we had experience with line agencies that thought that nothing had changed, so they went into old-style agreements and we had to say, 'No, there's a new world here and you've got to reconfigure your agreements.'

Mr English: As a postscript to that discussion, there is a publicly available document, which is the principles for the national partnership agreements which are on the Treasury's federal financial relations website.

Senator MOORE: Yes, I have seen it.

Ms Vroombout: It is the NP circular.

CHAIR: We have the COAG Reform Council, which is overseeing some part of this process. Perhaps the answer to my question is the National Reform Council, but please provide me with some clarity about my thinking here. Since this new process was introduced, has there been an audit, consideration or review of it in any way? It was supposed to be a more effective and efficient way of delivering funds to the states et cetera, so I suppose the question is: has it turned out to be more efficient and effective?

Ms Vroombout: Over the course of last year, heads of treasuries conducted a review of all of the agreements under the new framework, and they reported at the end of last year to the Ministerial Council for Federal Financial Relations, who then passed that report on to COAG. COAG considered the report in February this year. So, yes, there has been a look at how we are going with the new framework.

CHAIR: But that is a report undertaken by some of the principals involved: the party principals, in other words—the people who were actually intimately involved in negotiating the arrangements.

Senator MOORE: It is an internal review as opposed to an independent one.

Ms Vroombout: It is internal to government, but we did consult with portfolio agencies within both the Commonwealth and the states to get their perspective on how the new framework was going, and we consulted extensively between the Commonwealth and the states as to how it was going.

Mr English: In parallel, the COAG Reform Council also published its first progress on reform report, which is commissioned under the new framework, and in that it makes an assessment of the institutional arrangements under the reform agenda that COAG has put in place. It also reported for the first time in late 2010, and it similarly found that good progress had been made; that the focus on outputs and outcomes was an opportunity for states to pursue reform within jurisdictions in a meaningful way intended by the framework; and that we were still, I guess, part way down the path of achieving the goals of the Reform Agenda overall. A focus is needed on cultural change to get all parts of government working in a way that focuses more on outputs and outcomes. That was an independent view. It was, I think, a view formed with possibly not as extensive a process as the Treasury's

one was, but it was given as an independent piece of advice that was consistent with the findings of the work that Ms Vroombout has described.

Senator MOORE: Does the Intergovernmental Agreement on Federal Financial Relations have a review mechanism built into it? Does the agreement itself have a clause that talks about how it is going to be reviewed?

Ms Vroombout: My recollection is that the agreement itself does not, but there is a clause in there about review of the funding arrangements and the adequacy of funding under the agreement, and that clause says that such reviews should be conducted at least every five years.

Senator MOORE: So it is a five-year period. They vary. So this is a five-year one?

Ms Vroombout: Yes.

CHAIR: So the review that was undertaken and that Mr English has referred to was because someone said, 'Maybe we ought to have a review of this,' was it? Was it a serendipitous review, if I can use that adjective?

Mr English: Under the intergovernmental federal-state relations the CRC is commissioned to produce every year a report on progress of reform. Within that tasking it has defined that one of the things it will report on, and governments have agreed to this, would be the institutional structure that the FFR agreement has put into place. As well it looks at progress on implementing the other reform agendas that are embedded in the national agreement for the national partnerships.

Senator MOORE: That would be an annual review.

Mr English: Yes, that is an annual report.

Senator MOORE: Built into the general reform process it has been established there will be an annual review of how these agreements are going. So how it is going is agreed and then within the framework agreement there will be a formal review of adequacy and process every five years. So we have got two mirroring review processes for this particular process.

Mr English: Yes.

CHAIR: Does it mandate the kind of review that should take place, or just says a review?

Mr Perry: In which respect, Senator?

CHAIR: Of the five-year process.

Ms Vroombout: It does not set down the particular process, it just talks to there will be at least every five years a review of funding adequacy. The other point I would make is that the intergovernmental agreement tasks what will now be the standing council for federal financial relations with the ongoing monitoring and oversight of the federal financial relations framework. I guess at each meeting of the standing council they give consideration to how things are going, and that was what I guess created the impetus for the heads of treasuries review, so it was the ministerial council in its monitoring and oversight role that decided it was timely to step back a year after the framework had commenced and have a look at how it was going. I envisage that over time they may do that in addition to the reviews of funding adequacy.

CHAIR: I know that the COAG reform material is available on its website and the review they had done of the national partnership they have completed which has a reference to process in it. What about the rest of this review process you have been referring to? If I was interested to know what actually has been said beyond what you have told the committee today, where would I go to find out the nature of those reviews and the conclusions they reached, if anywhere?

Ms Vroombout: At the moment they are not publicly available. The heads of treasuries review report has not been made public. It was provided to COAG and there was reference to COAG's decisions in respect of it in the COAG communiqué, but at this stage it has not been made publicly available.

CHAIR: Is that a result of a decision not to make it publicly available or you just have not addressed that issue?

Mr English: I do not think we have had the specific request for it to date. However, in keeping with normal practice, if there was a need felt to release the report we would need to—

CHAIR: It is not so much a need as the fact, and I think Senator Moore made this point, that a lot of this activity takes place and most of it is not transparent. We have spent half an hour this afternoon trying to drag out some of the details because we are interested and we are doing a specific inquiry to understand the process. But other people and organisations may well have a strong interest and as a matter of good public policy, unless there is an argument about the need to maintain confidentiality—and, frankly, from what you have said you have not persuaded me that there is—then as a matter of good public policy these documents and these reviews ought to be

made available on your website or at least in a fashion which allows public access. I am pointing to the culture of this process, which seems to me to need some attention.

Senator MOORE: The decision maker on whether this review is public, would that be the new title of the ministerial council or standing committee for federal—

Ms Fitzpatrick: No, it would actually be COAG.

Senator MOORE: So it would be the heads of government.

Mr English: Heads of government.

Senator MOORE: So a decision on that would have to go back to COAG to make that determination.

Mr English: Certainly until the point decisions are made, we do try to operate in a manner consistent with the cabinet conventions. This is clearly not a cabinet process, but in our view governments need the capacity to have considerations and make decisions in a way that allows issues to be aired and frank advice to be given. Certainly the convention has long been that COAG documentation remains COAG-in-confidence until such time as a decision has been taken, then a decision is taken about the publication of the matter.

Senator MOORE: So it is a two-part decision: it is a decision on the issue and then a decision about whether it is going to be made public.

Mr English: That is usually the way it goes. It is not fixed in stone by any stretch. COAG has from time to time put out material of a deliberative nature to try to generate a response on the process it has created underneath COAG. In this case this report was prepared for COAG and taken to COAG and therefore we treat it in that way until we get a decision from COAG to the contrary. It is not unusual for material of that nature to be put out from COAG. Frequently some of the analytical work that we do is retained within government for the time being so that the continuing work is informed by it and not necessarily distracted by debate around material that was deliberative and not final. So what COAG has put out is the final review on the review, and there will be actions which we are all taking to follow up on it, which is COAG giving expression to the outcomes from the review. In this case my recollection is that there has not been a specific decision to release it, so we will not release it until we get that decision.

CHAIR: Do we have a COAG protocol that relates to transparency?

Mr English: I think I just enunciated the COAG protocol on transparency.

CHAIR: Is that written down in the protocols?

Mr English: I believe we did document the fact that COAG documentation would remain COAG-in-confidence until such time as there was agreement to release it. We have documented that much.

CHAIR: I have a couple of other matters before we finish. In relation to COAG and the setting of agendas, who does that? Who can set the agenda? Is there a difference between the business rules and the protocols in relation to setting the agenda?

Mr English: No, the business rules and the protocols continue the established pattern across prime ministers that the Prime Minister, at the end of the day, will set the agenda as chair of the meeting after a process of consultation with states and territories to garner their views about the issues that should be taken forward to the next COAG meeting. Typically we give effect to that by providing the Prime Minister with a letter some time in advance of COAG to sign to her colleagues to say: 'I am planning a COAG meeting for a particular date and the things I plan to put on the agenda at this stage are listed below. If you have other issues you think should be raised, now is the time to write and talk about it.' So it is collaborative but formally it is with the chair, as with most committee processes.

CHAIR: So the protocols make it clear that states can inscribe or suggest items for the agenda, do they?

Mr English: Yes.

CHAIR: But also acknowledge that the Prime Minister has the final determination on the content of the agenda. Is that also correct?

Mr English: I believe that is consistent with the language, yes.

CHAIR: In relation to these suggestions that there ought to be a more institutionalised COAG—in other words, not just your dozen people, Mr Perry in the department. There are various forms of agency, obviously. There is a full Commonwealth agency and a quasi-agency, with various consequences in relation to budgets and things of that kind. You are obviously working under the present arrangements. Is it obvious to you, or are there reasons why, we should be cautious about changing the structure that exists at the moment? Do you see any consequences, adverse or otherwise, that would follow from a more institutionalised foundation for COAG?

Mr English: We should say in advance of these comments that, if the government of the day took a decision to go with institutionalisation, we would work with that.

CHAIR: I understand that.

Mr English: In my experience the advantage that the current arrangements give is that COAG's work is inherently connected across the business of government and across the priorities of the Prime Minister in her domestic agenda, primarily, through the people who are working on the domestic agenda within the Prime Minister's department and, then, through that work, to the rest of the Public Service, most particularly Treasury but other elements as well.

I think an issue we would have to address in a more distinct institutional structure would be how to achieve that high level of integration that we currently have between the way an agenda is brought together and coordinated and the content of that agenda. All secretariats face that challenge. We have just been through a review of ministerial councils and their secretariats for COAG. It was not universally consistent across structures but it found that certainly those with small, dedicated secretariats suffered from being less engaged with the strategic issues confronting the ministerial council than those that had secretariats embedded with the policy people working on the issues that were to be considered by the council. That would be a challenge, for sure, and it is certainly one of the things that the current arrangements enjoy.

In terms of the level of effort that goes into looking after COAG, we try to exhibit quite a bit of organisational flexibility and make sure that what is needed is provided. I have at my disposal a division of between 40 and 50 people and, at times, we have moved people across the unit barriers, if you like, to ensure that COAG support was available. Again, it is one of the advantages of being part of a larger organisation, which in the case of PM&C is a few hundred people broad. So either arrangement would have its advantages, I suspect, but the move away from what we do currently would have that challenge to address.

Similarly, as a member of the department's senior executive my engagement with other members of the executive allows me to stay abreast of the whole of the government's agenda and how that has ramifications for COAG and things that the Prime Minister might have to take on. That would be harder for me to do if I were the head of an independent secretariat outside of Prime Minister and Cabinet. But, as I say, we would obviously support whatever direction government took.

CHAIR: I appreciate your position. Thank you, that is helpful. Does Treasury have a view about this?

Ms Vroombout: I guess we would share the same view as the Department of Prime Minister and Cabinet. We provide secretariat support for the Standing Council for Federal Financial Relations in the same sort of way as PM&C does for COAG, and we run it in a very similar way that PM&C runs COAG.

CHAIR: And how many people do you have dedicated to the task?

Ms Vroombout: There are probably about five, but within a division of about 30 and with support from the policy areas within Treasury. So I guess it is a similar sort of structure to the one that PM&C uses.

Mr English: To slightly extend the discussion, this is one of the challenges that confront the discussion around structuring and institutionalising the COAG agenda, support and timetable in that COAG is not a decision-making body of governments. It is a council of consensus so it reacts to the priorities that sovereign governments are dealing with on a day-to-day basis and its nature evolves over time with that. There is absolutely no question that there are many ways we could skin the cat in supporting COAG, but I think the experience of the 20 or 30 years of this brand of federalism we have been under suggests that you have a structure that evolves with the priorities facing COAG, and that works pretty well. Over time, COAG's focus has moved from, frankly, a fairly strong economic focus in the nineties. At the beginning of this century a broader range of issues around national security and the like came to the fore. Social policy issues have also come along over time. So to say that there is a business agenda that needs to be transacted every three months and that that must go forward come what may, regardless of the state of elections around the continent and the like, ignores the fact that this is a council by consensus. Therefore, we do our best to try and roll with the priorities that face governments as they come along.

Mr Perry: I would say too that COAG has shown itself to be quite nimble footed. I will give two illustrations of that. When we encountered the global financial crisis, at several days notice we brought on a COAG meeting in February of 2009 to consider the Nation Building and Jobs Plan. Then after the London transport bombings in 2005 it was the Victorian government that actually suggested to the then Prime Minister that we should have a COAG meeting to reconsider our counterterrorism arrangements and, again, that was brought on at very short notice.

Senator MOORE: I have a question that picks up a bit from your last comments. We had evidence from a witness this afternoon that, in his opinion, there was a discernible change in the dynamic of COAG after 9-11;

that the way the states, territories and federal government got together and responded to the security issues of 9-11 and made changes provided a dynamic that has flowed on to, as you described it, Mr Perry, the nimble-footedness of the organisation. I know it is impossible for you to give an opinion, but I am interested to know whether within the COAG members there was a confidence that things could move more quickly and reach agreement quickly in matters of urgency, as put forward by this witness this afternoon.

Mr Perry: I guess I could respond, because I have been around it longer than some. I would agree with that judgment or assessment, that 9-11 did focus COAG quite heavily at that time on counterterrorism and terrorism issues and the way in which we operate nationally. That led to changes, as you know, in legislation and a whole host of arrangements. Again, the unfortunate shooting at Monash University in Melbourne where a young student killed several other students led very quickly to the heads of government getting together and considering handgun controls. So there has been a great deal of impetus through the last decade in COAG.

Senator MOORE: Thank you.

CHAIR: I think we have exhausted ourselves! Thank you very much for your attendance before the committee today. It has been very helpful to our deliberations and we are grateful for the time you have given us. If we have any further questions we might send them along to you. You have taken a couple of matters on notice, Mr English, and if you can reply as soon as you can we would appreciate it.

Mr English: Of course.

CHAIR: Thank you very much.

Committee adjourned at 16:54