# THE PROSPECTS OF AUSTRALIAN FEDERALISM

NICHOLAS ARONEY

The frontiers of Australian federalism are potentially as numerous as the many ways in which federalism infuses Australian law and politics. There are frontiers about how we understand the very foundations of the federation, about what makes the *Australian Constitution* legally binding, and about how it can be altered in the future. There are frontiers in the practical working of our bicameral system of parliamentary representation – especially the Senate – and ongoing questions about its reform. There are also frontiers in the use by the Commonwealth of its legislative, executive and financial powers – a longstanding issue that has seen the scope and volume of federal legislation and administration grow in virtually every decade since federation. And there are frontiers in the relations between the federal, state and territory governments – a murky landscape, in which not all that happens is open to public view or democratic accountability.

In each of these respects our federal system displays a kind of path dependency. By 'path dependency' I mean the phenomenon that the future decisions open to an individual, a group of people, an institution, or an entire society are often controlled by history – they are shaped and constrained (not inexorably, but effectively nonetheless) by patterns of behaviour and institutional decisions settled in the past.[1] These patterns of behaviour and causal patterns have a tendency to lock-in particular institutional pathways that cannot easily be overcome.

Let me give some examples of path dependency in Australian federalism. I'll begin with processes of formal constitutional change.

## I CONSTITUTIONAL CHANGE

The amendment clause in the *Constitution* (section 128) stipulates that it can only be amended pursuant to a law passed by the Parliament and approved by the people in a referendum at which a majority of Australian voters and a majority of voters in a majority of states approve of the change. This seems to be an even-handed process which is both democratic and federal in its underlying principles. However, in practice, it is a process that effectively limits formal constitutional change to proposals initiated or supported by the federal government. The states cannot initiate formal constitutional change, nor can the people.

It is true that amendment proposals have to be passed by the Parliament, and they can under section 128 be initiated by the Senate without the support of the House of Representatives.[2] However, no such proposal has ever been put to the people. When the Senate passed two bills to amend the *Constitution* in 1914, not only did the House of Representatives fail to pass the bills, but the Governor-General, acting on the advice of the federal government of the day, declined to submit the proposed amendment to the voters.[3]

In practice, proposals to amend the *Constitution* are inevitably initiatives of the federal government. This effective monopoly has meant that the preponderance of proposals that have gone to referendum have involved an increase in federal power in one way or another.[4] And this in turn has contributed to the unpopularity of such proposals. Lacking consensus support, the proposals have most often failed the first

referendum hurdle – a majority of Australian voters – let alone the second hurdle of a majority of voters in a majority of states.

Even attempts to reform the amendment process itself in order to open it up to the initiative of the states have failed, precisely because the federal government has not been prepared to give up its monopoly. For example, the Constitutional Commission of 1988 recommended that half the states, representing a majority of Australia's population, be enabled to initiate a referendum.[5] But the Commonwealth chose not to implement the recommendation. Why, after all, would it see the need to give up its monopoly?

## II FEDERAL LEGISLATION

A similar path dependency characterises the Commonwealth's exercise of its legislative powers and the High Court's approach to interpreting the constitutional division of power. The common law doctrine of precedent institutionalises a kind of path dependency: past cases constitute authoritative determinations which bind decisions in the future. Having adopted in the *Engineers' Case* in 1920[6] an approach to the interpretation of the scope of Commonwealth legislative powers that does not concern itself with reserving any fixed set of powers to the states or with maintaining some kind of 'federal balance' between them,[7] the High Court has committed itself to interpreting each head of Commonwealth legislative power as widely as the words used can reasonably sustain.[8] All that the Court looks for in a federal law is a 'sufficient connection' to the subject matter of a head of power; it does not matter if the material substance of the law is concerned with some topic that lies outside the Commonwealth's stipulated powers.[9]

This method encourages Commonwealth lawmakers to press the frontiers of Commonwealth legislative power whenever it is politically expedient to do so. Take as an example the Rudd Government's *Australian Charities and Not-for-profits Commission Act 2012* (Cth) ('*ACNC Act*').[10] This law introduced a Commonwealth-level regulatory framework for the not-for-profit sector, and established the Australian Charities and Not-for-profits Commission ('ACNC') as the new sector regulator. The ACNC is empowered under the Act to compel the publication of information, to give directions to charities, and in some circumstances to remove and replace their leadership. In addition, the Regulations require registered charities to meet an array of 'governance standards',[11] several of which are vague and at times awkwardly expressed.

There is nothing in the *Constitution* to suggest that the regulation of not-for-profit entities such as charities was intended by the framers to fall within Commonwealth legislative power.[12] The closest provision is the corporations power, which extends to the regulation of 'trading corporations', 'financial corporations' and 'foreign corporations'.[13]

Conceived as 'types' or 'categories' of corporation, these invite comparison with other very different categories of corporations, such as those formed for 'municipal', 'religious' or 'charitable' purposes.[14] But that has not stopped the High Court, consistent with its received method of constitutional interpretation, from finding that the corporations power extends to the regulation of *any* corporation that engages in sufficiently significant 'trading activity', even if its main purposes and predominant activities are of a non-trading character – as is the case for most not-for-profit charities.[15] This approach has enabled the Commonwealth to use the *ACNC Act* to regulate charities that happen to be corporate in form and engage in

sufficient trading activities. Indeed, in the *ACNC Act*, the Commonwealth has gone even further, regulating charities that are not organised as corporations by relying on a combination of several other heads of power, including the taxation, external affairs and broadcasting powers.

Let me focus on one aspect of the law to illustrate what I mean. Among other things, the *ACNC Act* establishes an electronic database of registered entities to be made available for public inspection on the internet. This register includes information about each charitable entity, such as its name, its Australian Business Number, its directors and trustees (as applicable), its financial reports and other statements containing information about the entity.[16] In the Revised Explanatory Memorandum that accompanied the Act, the Commonwealth argued that what it calls the federal 'communications' power supports the establishment of the database and the empowering of the ACNC to obtain the information and to undertake monitoring for the purpose of determining whether information provided by an entity is correct.[17]

Notably, the *Constitution* does not anywhere refer to a 'communications' power. What it does refer to, in section 51(v), is a power to legislate with respect to 'postal, telegraphic, telephonic, and other like services'. The High Court has held that these 'other like services' include radio and television broadcasting.[18] The Commonwealth also appears to have relied on this head of power to support regulation of aspects of the internet.[19] The cases have held that the head of power enables the Commonwealth to control the provision of such services by establishing a broadcast licensing system that prescribes conditions for the holding of such licenses, which conditions can include controls on the content that is communicated using such services, provided there is a proportionate relationship between

the purposes of the legislation that connect it to the head of power and the means adopted by the legislation to achieve those purposes.[20]

Such laws regulate the provision and use of broadcasting and telecommunication services and it is possible to characterise them as laws that regulate those particular types of technology considered as 'services' provided to the public. However, the relevant section of the *ACNC Act*,[21] interpreted in the context of the Act as a whole, is not a law that regulates the provision and use of such 'services'. Rather it prescribes that certain information is to be made available for public inspection, and it just happens to make use of the internet as an effective way in which the information can be disseminated. This use of the internet is the only connection between the law and the relevant head of federal legislative power.

It seems to me that there are real questions to be asked whether there is a sufficient connection between the law and the head of power in this instance.[22] And there is even less constitutional justification for the requirement in the Governance Standards established by the *ACNC Regulations* that compels charities to 'make information about [their] purposes available to the public, including members, donors, employees, volunteers and benefit recipients'.[23]

The *ACNC Act* is a recent example of the Commonwealth pressing its legislative powers to their extreme frontiers. But in the absence of a constitutional challenge to the legislation, it is only because there is currently a government-commissioned inquiry into the Act that some of these issues may possibly be addressed.

## III INTERGOVERNMENTAL RELATIONS

Relations between the Commonwealth and the states display another kind of path dependency. The key to understanding this, I suggest, is to focus on the financial powers and capacities of the Commonwealth and the states.

At the time of federation, the major source of taxation revenue for governments was in the form of taxes on goods – in particular, customs duties imposed on the importation of goods. For various reasons associated with the establishment of free trade within Australia and the deferral of the question of free trade with other countries to political determination at a federal level, it was decided that the Commonwealth should have exclusive power to impose not only duties of customs, but also excise duties.[24] This meant that the states would lose a major source of their income, and so transitional provision was made for the temporary distribution of surplus Commonwealth revenue to the states (section 93 of the *Constitution*) while a permanent provision (section 96) authorised the Commonwealth to make financial grants to the states on the terms and conditions that it thinks fit.[25] Alfred Deakin, one of the framers, saw the implication very early. He observed that it would be the 'power of the purse' that would ultimately establish the dominance of the Commonwealth over the states. He put it this way:

> As the power of the purse in Great Britain established by degrees the authority of the Commons, it will ultimately establish in Australia the authority of the Commonwealth. The rights of self-government of the States have been fondly supposed to be safeguarded by the Constitution. It left them legally free, but financially bound to the chariot wheels of the Central Government. Their need will be its opportunity. The less populous will first succumb; those smitten by

> drought or similar misfortune will follow; and finally even the greatest and most prosperous will, however reluctantly, be brought to heel. Our Constitution may remain unaltered, but a vital change will have taken place in the relations between the States and the Commonwealth. The Commonwealth will have acquired a general control over the States, while every extension of political power will be made by its means and go to increase its relative superiority.[26]

While Deakin did not foresee the rise of personal and corporate income tax as another key source of government revenue, his prediction has proven remarkably prescient. Without going into the detail, today it is the case that the states only raise about half of the money they spend for the provision of services (for example, on health, education, transport, policing), while the remainder comes to them in the form of Commonwealth grants, a further half of which is tied to conditions imposed by the Commonwealth.[27] This imbalance between the raising of revenue by the Commonwealth and the spending of the revenue by the states is called 'Vertical Fiscal Imbalance'. Moreover, the conditions imposed on many of the grants by the Commonwealth require the states to provide detailed reports which enable the Commonwealth to assess whether they have achieved certain benchmarks. This system of reporting and benchmarking is ostensibly agreed to between the Commonwealth and the states and is meant to improve the democratic accountability of governments to the people. But it seems to an outsider that in practice it is the Commonwealth that drives the process and holds the states to account.

These sorts of issues were frankly addressed in a series of Issues Papers prepared in association with former Prime Minister Tony Abbott's recent attempt to initiate a root and

branch reform of the Australian federal system. With remarkable candour, *Issues Paper 1* observed that the financial relationship between the Commonwealth and the states had the effect of: reducing state autonomy through the use of tied grants; undermining state certainty over revenue allocations; reducing transparency and accountability to citizens; increased duplication and overlap; and weakened incentives for tax and microeconomic reform by the states.[28]

*Issues Paper 5* observed that high Vertical Fiscal Imbalance between the Commonwealth and the states further encourages what it described as blame-shifting, fiscal illusion and moral hazard.[29] Blame-shifting occurs when each level of government denounces the other for inadequacies in service provision. The Commonwealth blames the states for incompetence and ineptitude. The states blame the Commonwealth for insufficient funding. Fiscal illusion arises when states engage in the over-provision of services without facing the political cost of raising additional revenue through taxes or borrowing. And a kind of moral hazard is evident when political pressure is placed on the Commonwealth to bail out a state that is facing fiscal problems, thereby rewarding fiscal irresponsibility.

The White Paper process initiated by the Abbott Government was merely the latest in a long line of attempts to reform the Australian federal system. Less than a decade earlier, the Rudd Government had initiated and secured a new Intergovernmental Agreement on Federal Financial Relations (2008) that was meant to end the 'blame game', improve the provision of government services and make governments more publicly accountable.

However, reviewing the situation just a few years later, the Abbott Government's *Issues Paper 1* observed that the principles of the Intergovernmental Agreement on Federal

Financial Relations were 'not being honoured by either the Commonwealth or the States and Territories. Cooperative federalism was again shifting towards coercive federalism'.[30] The sorry process was described in this way:

> Using conditional grants under section 96 of the Constitution, the Commonwealth puts a sizeable and difficult-to-resist sum of money on the table as an inducement to States to shape their policies in ways that align with the Commonwealth's view of what the 'agreed' priorities should be in a particular area of activity. As States and Territories seek to secure [this] funding, they surrender a degree of autonomy to pursue their own preferences.[31]

Recognising the significant power disparities between the Commonwealth and the states, the Issues Papers flagged various ways in which the imbalances and dysfunctionalities could possibly be remedied. One of these involved deliberate reallocation of responsibilities between the Commonwealth and the states in a manner suitable to contemporary circumstances and expectations. However, the Issues Papers recognised the difficulties involved. They observed that:

> devolving responsibility to [a] lower level of government is not necessarily something that comes easily. In a situation where the Commonwealth is heavily involved in many areas of activity, and therefore is held politically accountable for outcomes and for the efficient expenditure of taxpayers' money, the temptation to trust less and control more can be very strong for ministers and public servants alike. [32]

Here the Issues Papers candidly acknowledged the path dependent situation in which the Australian federal system finds itself. But the problem was even more deeply rooted than this. For, without any sense of irony, the Issues Papers referred to

these responsibilities as being 'devolved' to the 'lower' levels of government. This is not the language of federalism but of devolution. It is the language that one encounters in unitary states, like the United Kingdom, which have gone through the process of devolving formerly centralised powers on constitutionally 'lower' levels of government. But in an integrative federation such as Australia the responsibilities were originally those of the constituent states and it was the states that decided to transfer some of their powers to the federal government, not vice versa. However, characterising the issue as a matter of devolution, the Issues Papers reflected and contributed to the very problem they were trying to solve! Despite all the good intentions, therefore, it came as no particular surprise that the Federal Government's noble attempt to reform the federal system ended in abysmal failure.

As I have tried to show in other work,[33] there are lessons to be learned from other federal countries, such as Germany, Austria and Switzerland, concerning the ways in which federal systems can effectively be reformed. In the light of that overseas experience it seems to me that the path dependent problems Australia faces are related to two features of Australian politics.

The first of these is the cyclical nature of the Australian political system. As the instructive experience of Switzerland especially suggests, successfully reforming a federal system takes a long time to achieve. The reform process has to be sustained over the life of more than one electoral cycle. But the highly partisan nature of our politics means that reform efforts initiated by one government are not going to be promoted or maintained by their political opponents. If Australian federalism is to be reformed, some way of overcoming this problem will need to be found.

The second problem is the tendency of Australian politics to pragmatism. While the Issues Papers undertook a refreshingly candid assessment of the state of the federal system, and while they laid out a very laudable set of principles according to which the system should be reformed, there was also a characteristically Australian pragmatism on view. The Issues Papers very quickly moved from 'principle' to 'practice' in a manner that short-circuited any attempt to secure sufficient agreement on principles before moving to the practicalities of what reform would actually mean. But moving so quickly to the practicalities encourages the participants to revert to thinking about the issues in terms of their one-sided interests rather than the benefits to be secured through a reform of the system as a whole.

In these ways, the Abbott Government's White Paper process demonstrated, once again, the path dependent nature of Australian federalism. The ideals of the White Paper process were to increase democratic participation, but the 'governmentality' of Australian federalism ultimately prevailed: citizens were more often seen as 'clients' of government services than as 'participants' in their own self-government. The White Paper process was intended to set out a measured, deliberative approach to reforming the system, but in the end, the process was not able to survive a change in political leadership within the same political party. When Prime Minister Malcolm Turnbull proposed that the federal government would reduce its income tax by an agreed percentage and allow state governments to levy an income tax equal to that amount, the states, especially the Labor states, declined the invitation.

Although the idea had been canvassed in the Discussion Papers, some, quite unfairly, denigrated it as a 'thought bubble'.[34] But even though the reactions to the Prime Minister's

proposal were politically exaggerated, the whole affair illustrates the fundamental problem with executive-led reform efforts: they are too prone to politicisation.

## IV CONCLUSIONS

The collapse of the White Paper process was, in the scheme of things, sadly predictable. This is because a kind of path dependency characterises Australian federalism. As Jorg Broschek has observed of federal systems generally:

> Institutional legacies can profoundly shape the patterns of federal reforms. Path dependence situates reform proponents and opponents within an institutional environment that is rooted in earlier developments. Demands for change are filtered and translated into distinct reform patterns.[35]

This filtering and translating has meant that past attempts to reform the Australian federal system have often ended up reinforcing the tendencies of the system in its characteristic centralism and governmentality.

Path dependency can have multiple causes. Institutional patterns can become entrenched because they are supported by an elite group of political actors whose interests they serve. However, they can also become entrenched because the very same patterns are believed to be morally just or legitimate, or because they are thought to play a necessary or unavoidable role within the political system as a whole.[36]

Unravelling the causes of Australia's path dependent federal system is therefore important, and care needs to be taken when trying to reform the system. For it can often be counter-productive to pursue changes directed to transforming a constitutional system into an ideal but ultimately impossible or

highly improbable state of affairs, for a halfway house between present reality and the unattainable ideal may be worse than the status quo.[37]

The experience of other federations suggests ways in which it may be possible to reboot the Australian system, but this would require a different attitude on the part of our governments, one which seeks to build long-term consensus instead of short-term partisan gain. For the moment, however, Australian federalism is trapped in a rut and there appears little that we in the present can do about it. At the least, it is important that we try to understand the path dependent patterns that have determined the development of our federal system. Without such an understanding our attempts to reform the system are unlikely to be successful and could easily prove to be counter-productive.

## Endnotes

1 Paul Pierson, 'Path Dependence, Increasing Returns, and the Study of Politics' (2000) 94(2) *American Political Science Review* 251; Scott E Page, 'Path Dependence' (2006) 1 *Quarterly Journal of Political Science* 87.

2 That is, pursuant to a deadlock-breaking procedure in s 128 of the *Constitution*.

3 George Williams and David Hume, *People Power: The History and Future of the Referendum in Australia* (UNSW Press, 2010) 41–42.

4 According to Williams and Hume, above n 3, 24 (out of 44) proposals would have increased the power of the Commonwealth. This is a conservative assessment.

5 Ibid 29.

6 *Amalgamated Society of Engineers v Adelaide Steamship Co Ltd* (1920) 28 CLR 129.

7 *New South Wales v Commonwealth (Work Choices Case)* (2006) 229 CLR 1, 73.

8 For more detail, see Nicholas Aroney, Peter Gerangelos, James Stellios and Sarah Murray, *The Constitution of the Commonwealth of Australia: History, Principle and Interpretation* (Cambridge University Press, 2015) 133-136, 179-181.

9 Ibid 136-143, 150-157.

10 For more detail, see Nicholas Aroney and Matthew Tumour, 'Charities Are the New Constitutional Law Frontier' (2017) 41(2) *Melbourne University Law Review* 446.

11 *Australian Charities and Not-for-Profits Commission Regulation 2013* (Cth).

12 In fact, all the evidence suggests that the opposite was the case.

13 *Constitution*, s 5l (xx).

14 *Huddart, Parker & Co Pty Ltd v Moorehead* (1909) 8 CLR 330, 393-5 (Isaacs J).

15 *R v Judges of Federal Court of Australia; Ex parte Western Australian National Football League (Inc)* (1979) 143 CLR 190.

16 *ACNC Act*, s 40–5(4).

17 Revised Explanatory Memorandum [2.3]–[2.6].

18 This was itself a stretch. See *R v Brislan; Ex parte Williams* (1935) 54 CLR 262; *Jones v Commonwealth (No2)* (1965) 112 CLR 206.

19 For example, see *Broadcasting Services Act 1992* (Cth), Schedule 5; *Interactive Gambling Act 2001* (Cth).

20 *Nationwide News Pty Ltd v Wills* (1992) 177 CLR 1.

21 Section 40-5(4).

22 For more detail, see Aroney and Tumour, above n 10.

23 *ACNC Regulation* reg 45–5(2)(b).

24 Cheryl Saunders, 'Fiscal Federalism-a General and Unholy Scramble' in Gregory Craven (ed), *Australian Federation: Towards the Second Century* (Melbourne University Press, 1992) 101, 103-4.

25 See also s 94 in relation to surplus distributions, entirely in the discretion of the Commonwealth.

[26] Anonymous column written by Alfred Deakin in the *Morning Post* (London, 1902).

[27] *Reform of the Federation White Paper: A Federation for Our Future: Issues Paper 1* (Commonwealth of Australia, September 2014) 51-53 (Figures 68); *Reform of the Federation White Paper: Coag and Federal Financial Relations: Issues Paper 5* (Commonwealth of Australia, February 2015) 31 (Figure 3.4).

[28] *Issues Paper 1,* 32. See also *Issues Paper 5,* 32-34.

[29] *Issues Paper 5,* 33.

[30] *Issues Paper 1,* 12.

[31] *Issues Paper 1,* 19.

[32] *Issues Paper 1,* 20.

[33] For more detail, see Nicholas Aroney, 'Federalism and Subsidiarity: Principles and Processes in the Reform of the Australian Federation' (2016) 44(1) *Federal Law Review 1* and Nicholas Aroney, 'Reforming Australian Federalism: The White Paper Process in Comparative Perspective' in Mark Bruerton et al (eds), *A People's Federation* (Annandale, NSW: The Federation Press, 2017) 199.

[34] Australian Senate, Finance and Public Administration References Committee, *Outcomes of the 42nd meeting of the Council of Australian Governments held on I April 2016* (Canberra: Commonwealth of Australia, May

2016); Senator Penny Wong Twitter Account (26 April 2016).

35 Jorg Broschek, 'Pathways of Federal Reform: Australia, Canada, Germany, and Switzerland' (2015) 45(1) *Publius: The Journal of Federalism* 51, 68.

36 James Mahoney, 'Path Dependence in Historical Sociology' (2000) 29(4) *Theory and Society* 507, 515--526.

37 Lawrence Solum, 'Constitutional Possibilities' (2008) 83(1) *Indiana Law Journal* 307, 327-8.