
14 Commonwealth–State benchmarking and the state of Australian Federalism*

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14.1 Introduction

Like any good public servant, I want to start by managing expectations.

I think you would all agree that Commonwealth–State benchmarking and the state of Australian Federalism are not topics that naturally lend themselves to a high-wire comedy act. At the same time, however, you can rest assured that I will not try your patience with a basic seminar on benchmarking and federalism in Australia.

Instead, tonight I want to draw on my experiences from two of the defining Council of Australian Government (COAG) reforms of the past few years to make a more general, integrated and, I think, more interesting point. The two COAG reforms I will be drawing on are the post-2008 federal financial relations framework and the competition and regulatory reform agenda. In reflecting on these reforms and my related experiences of COAG meetings, there can be no doubt that these gatherings of government leaders in Australia have provided no shortage of personalities, fast-moving politics and grand drama.

We have had some vigorous debates on particular issues and we will have them again. That is the nature of robust public policy making and it should be welcomed. But beyond these immediate and attention-grabbing events, over the past years we have agreed on some fundamental backstage reforms to the way governments work together.

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COAG has started to institutionalise the sort of policy and governance disciplines that we adopt within our own governments and that are also shaping best practice overseas. My main point tonight is that these shared practices — which I will describe as a strategic policy logic of outcomes-based, evidence-driven benchmarking and a genuinely federal approach to national governance — will survive the highs and lows of Commonwealth–State relations because, in short, good processes get good outcomes.

14.2 The common features and shared strategic policy logic of benchmarking and federalism

Before I draw on some COAG case studies to illustrate this central theme, I need to give credit where it is due. By bringing these two topics together, the Productivity Commission and the Forum of Federations have shown a lot of practical wisdom.

Without renegeing on my promise not to rehearse the benefits of benchmarking and federalism, it is useful to draw out their mutually reinforcing features and shared strategic purpose. We are all familiar with the rationale for benchmarking, in promoting public accountability, comparative learning and competitive performance assessment. Similarly the public benefits of a federal structure of government, in enabling flexibility, diversity, accountability, competition and innovation, are well known.

Clearly, benchmarking is not a passing fad, just as federalism is not an evolutionary stage on the road to unitary government or something that we can ‘fix’ once and for all. Instead, when we reflect on how benchmarking and federalism work together, we see that these approaches to public policy and national governance actually help us to understand and deal strategically with contemporary problems.

Taken together, benchmarking and federalism promote policy rigour, encourage good government and help us provide better outcomes for citizens. They also share important practical similarities, in that they both can be incredibly difficult in practice, their value is not always well understood by key stakeholders, and neither is done for its own sake.

My aim tonight is to explore these intersections and similarities and, in doing so, to demonstrate that a deliberate and integrated approach to benchmarking and federalism is simply part and parcel of being evidence-based in our policy analysis and self-consciously systematic in our governance arrangements.

14.3 How Vertical Fiscal Imbalance distorts Commonwealth–State relations and national strategic policy

Before I move on to my case studies, however, I need to name the ‘elephant in the room’: the excessive disparity that exists between the Commonwealth’s superior revenues and the States and Territories’ direct infrastructure, service delivery and associated spending responsibilities. We all know this elephant by its nickname, vertical fiscal imbalance (or VFI), and we all know that it is the main cause of difficult negotiations, blurred roles and responsibilities, and media and public misunderstanding.

For our international visitors tonight, let me briefly summarise the Australian version of this common federal fiscal dilemma. Some mismatch between a central government’s tax-base and regional governments’ spending responsibilities is not unusual, and might even be desirable. Unfortunately, in Australia the fiscal imbalance between the Commonwealth and the States and Territories is vast. The Australian federation has the dubious honour of competing for the most extreme VFI in the world. In Victoria nearly 50 per cent of our \$46 billion State budget comes from the Commonwealth. Some other Australian jurisdictions are even more dependent on the Commonwealth for revenue.

Excessive VFI has the potential to undermine an evidence-based and rigorous approach to the distribution of public accountability in a range of policy areas. It does not make centralisation inevitable, but it does encourage opportunistic appeals for federal interventions and can contribute to a principal–agent attitude to federal relations.

14.4 First case study: the IGA FFR

Having recognised these challenges, I’d like to turn to my first COAG case study: the 2008 federal funding reforms. This case study provides us with a valuable illustration of how — despite VFI — we have nonetheless started to institutionalise a better way of working together.

I’ll summarise these reforms briefly for our international visitors. The *Intergovernmental Agreement on Federal Financial Relations* — the FFR framework — has established a national outcomes-based funding and performance regime. It covers six key policy and services areas, including health and education, while also providing a clear articulation of the principles for future cooperation.

A mere two years ago, the Australian federation did not have a robust and reform-enabling framework for federal financial relations. Now we have a centralised process for administering payments to the States and agreed core funding on an *ongoing* basis. This means we should be able to avoid fights every five years over new funding agreements. The Framework also provides for reform pilot initiatives which, if successful, could subsequently be rolled into the core funding. These were hard won gains.

This focus on outcomes-based funding has been matched with greater performance reporting. The FFR framework empowers the independent COAG Reform Council (CRC) to publish performance information against outcomes annually for *all* jurisdictions. These reports are major steps towards better national benchmarking and more meaningful public accountability. Stakeholders, the national media and the general public are becoming more aware of them, and no jurisdiction — the Commonwealth or a State or Territory — will be able to hide when a CRC report reveals poor comparative performance.

The FFR framework continues the strategic policy logic of benchmarking and federalism, and it forces us to continually improve on the key outcome metrics that matter to the public. These reforms — the focus on outcomes rather than input controls, and the incentives for innovation — have been significant. But they have, at times, been lost in wider public debates on COAG and its reform agenda. Unfortunately, some reports in the national media present performance reporting under the FFR framework as an exercise in the ‘blame game by other means’.

Data quality issues in particular present a shared challenge, but often media reports on these issues are framed as the Commonwealth ‘pushing’ States and Territories to release information and raise their performance. In reality, working through these issues and refining agreements will take time and more pro-active governance by all jurisdictions.

We need, as the CRC Chairman has recently said in relation to their report on COAG’s overall progress, to sustain our efforts in fully implementing these far-reaching reforms. I am confident that the FFR framework will have a significant, long-term and positive impact on the quality of intergovernmental cooperation — and, in turn, a positive impact on the quality of Australian public policy and government services.

14.5 Second case study: the competition and regulatory reform agenda

For my second case study, I want to reflect on an important substantive component of COAG's agreed reform agenda — competition and regulatory reform. This case study takes our reflection on the shared strategic policy logic of benchmarking and federalism in a slightly different direction, by demonstrating how we need to apply these disciplines when weighing up — on a case-by-case basis — the relative costs and benefits of regulatory competition, mutual recognition, harmonisation and centralisation.

Prior to COAG's most recent reform agenda, it had been argued by some that competitive federalism in Australian regulatory systems had failed, and that States and Territories should instead resist parochialism and embrace market reforms in the national interest. Since then, COAG has made good progress on extending and completing its previous competition and business regulation reform agenda through a new *National Partnership Agreement to Deliver a Seamless National Economy*.

Reflecting on those debates and these cooperative reforms, it seems to me that arguments based on 'parochialism versus the national interest' do not do justice to either the case for national market reforms or the reform-enabling potential of competitive federalism.

As should be clear from what I have said tonight, our commitment to federalism is not based on a parochial or abstract commitment to States' rights. Instead, it is a commitment to context-sensitive, deliberative, accountable and right-sized governance.

Where a rigorous and evidence-based cost-benefit analysis supports a centralised approach — even a referral of powers — then of course that is the approach we should take. The national systems for business name registration and Standardised Business Reporting are good examples of this, just as the case for advancing a lot of the Seamless National Economy agenda was well established. More generally, and as scholars of federalism well know, the need for cooperation in a federal system can reinforce the case for such reforms, by demonstrating their broad-based support across governments and thus building their public legitimacy. COAG acted as a catalyst for change in this case and that is a positive message.

Equally, however, where the siren song of centralisation risks leading us into a uniform *but counter-productive* national regulatory regime, we should collectively pause and take stock of the real costs involved. There is nothing automatically more efficient about having uniform and centrally-controlled regulatory regimes for every product or service market that has a national dimension. A uniform regime, that adopts the wrong regulatory settings or approach, can be much more costly to the

national economy than having eight separate regimes. Equally, the choice to have a uniform national scheme necessarily stifles innovation, both by preventing jurisdictional experimentation and by potentially requiring a further round of multilateral negotiations before a cooperative scheme can be adjusted in light of experience or changing circumstances.

Without pre-judging the case, we should always start our shared thinking from first principles, by clearly articulating our common regulatory goals and weighing up the costs and benefits of how to get there. In this area, like others, we should apply good strategic policy logic by drawing on real-world evidence and being self-consciously systematic in our governance arrangements.

14.6 Concluding thoughts

In closing, I want to return to the practical wisdom in the theme for this roundtable. We have learned a lot about getting the most out of benchmarking and federalism in the last few years.

The COAG reforms that I have discussed tonight demonstrate the growing role in the Australian federation for a strategic policy logic focused on outcomes and facilitated by evidence-based benchmarking and a deliberative approach to national governance. Overall, I think we have started to embed the shared institutions and culture upon which the governments of our federation can develop and deliver better policy and service outcomes for all Australians.

Given my emphasis tonight on how good processes support good outcomes, it should not surprise you that I regard ongoing institutional reform of COAG itself as important. COAG provides the governments of Australia with a shared strategic decision-making and coordination forum. To deliver on this role, I would like to see COAG adopt and formalise some basic procedural disciplines, such as planning for a small number of regular meetings each year. Similarly, COAG needs an independent secretariat to coordinate a more focused agenda and allow for the States and Territories to put issues on the table for discussion and action. To underpin such changes, I think an intergovernmental agreement enshrining COAG's principles and governance would be a very positive step.

The undeniable merits of good processes in supporting good outcomes are such that I think systemic reform of COAG's operations, and a better focus of our collective efforts on key shared national challenges, is a real possibility in the near term.

I hope my thoughts this evening are useful to your conversations over the next two days. I look forward to hearing the outcomes of these productive discussions.