

Chapter 8

Designing Intergovernmental Grants to Facilitate Policy Reform

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I Introduction

The challenge within federal systems is that the policy goals of national government are often in conflict with those of sub-national governments. For the national government, improving economic efficiency is a priority and this has become synonymous with uniformity and the need to harmonise policies across the federation. At the same time, its focus on equity has led to the funding of the federation in a way which addresses differences in revenue capacity and cost disability across sub-national governments. In most federations, what has resulted is not only a diminution of social and economic differences over time, but less tolerance for any diversity, including that arising from competition across the federation.

This trend is troubling since while uniformity can encourage free trade and labour and capital mobility both internally and internationally, it can also remove the incentive for sub-national governments to engage in innovation and experimentation. Optimally, the benefits of uniformity will be balanced against the benefits that diversity and competition bring to a federation.

This chapter makes two arguments: first, that Australia's current grant allocation framework is in conflict with the general push for uniformity across states; and second, that it is possible to reform the existing grant allocation framework in a way that makes it better able to accommodate both uniformity *and* diversity within the federation. Such a framework would also have the advantage of ensuring that cooperative federalism does not remove the incentive structure for sub-national governments so necessary for positive benefits to arise from competitive federalism.

The chapter begins with an overview of the Australian federation's performance against the criteria of efficiency, equity, accountability and transparency. It is argued that addressing these criteria need not be at the cost of diversity. Just why this is the case requires an understanding of the conceptual issues guiding

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