THE STRANGE (CONTINUING) STORY OF COMMONWEALTH AUTHORITY TO SPEND

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This paper deals with the source of authority for the Commonwealth's power to spend and, by extension, to contract. It involves Alfred Deakin, at least peripherally, and to that extent complements Professor Judith Brett's paper. The issues that it raises are familiar in other countries as well. But as they have developed here, the story has taken some distinctively Australian twists, and is still playing out.

Australia became a federation as a way of uniting six colonies in a 'nation for a continent and a continent for a nation', as the catch-cry went. From that perspective, Australia was an (almost) classic 'coming together' federation. Union has long since been achieved, however. The contemporary challenge is to realise the potential of federalism for Australian democracy across an area that is geographically vast, with diverse needs and attitudes, in a political culture that is not well-attuned to consultation, negotiation and power-sharing.

The federalism provisions of the *Constitution* are modelled closely on those of the United States, in key respects. In fact, however, Australia was, and is, quite different to the United States in many ways that affected the fit of the US model. One of these was the dependence of the Australian colonies, about to become States, on customs and excise as sources of revenue. The emphasis that the framers of the *Constitution* placed on internal free trade meant that duties of customs and also, or so they thought, duties of excise, needed to be exclusive Commonwealth powers. How to deal with the impact of that

change on the budgets of the States occupied more time of the framers of the *Constitution* than any other issue.

Despite their labours, in the end, with hindsight, the result was unsatisfactory; made even worse by some last minute changes at a Premiers' Conference in 1899. Transitional provisions for revenue redistribution managed the problem for the first 10 years (secs 87, 89, 93). After that, the only continuing guarantee was a requirement in section 94 for the Commonwealth to redistribute to the States, monthly, its 'surplus' revenue; a requirement that was quickly circumvented by accounting practice.[1] Thereafter, the only basis for revenue redistribution was the power for the Commonwealth to make grants to the States under section 96; a section added to the draft in last-minute negotiations, which apparently was intended to be transitional, but which in practice now is permanent. This is the context in which Alfred Deakin famously remarked, in an anonymous letter to the *Morning Post* in 1902, that federation left the States 'legally free, but financially bound to the chariot wheels of the central Government'.[2]

The use of this familiar quote almost always assumes Deakin's prescience. Indeed, the letter as a whole seems to speak accurately to current conditions, if read through a contemporary lens. But Deakin could not possibly have foreseen the manner in which this imbalance between legal power and financial muscle would play out in Australia, and with what practical consequences.

For a period, in fact, after the Financial Agreement of 1927, the States were independent of the Commonwealth for general revenue redistribution. But that balance changed dramatically after World War Two, initially through the uniform income tax scheme and gradually through the expanded judicial understanding of duties of excise. These two developments left

the main sources of revenue in the hands of the Commonwealth, de facto or de jure. The bases for general revenue redistribution, including inter-state equalisation, have been an ongoing problem ever since.

The effect of the fiscal imbalance on Australian federation is a well-known story that I do not pursue here. Rather, my purpose is to draw attention to one other consequence of the imbalance: the encouragement that it offered the Commonwealth to rely on its considerable revenues to expand its authority into areas of State responsibility.

One obvious vehicle for the purpose is the Commonwealth's power under section 96 to grant financial assistance to the States on such terms and conditions as the Commonwealth Parliament thinks fit. Increasingly, however, the Commonwealth has by-passed the States, relying on direct spending in areas where its legislative powers are, at best, doubtful.

Typically, such programs rely solely on executive action, apart from a (usually very) general appropriation by the Parliament. Sometimes they are, effectively grants, accompanied by (often detailed) executive guidelines; sometimes the vehicle for expenditure is contract. This has become an attractive model, for successive Commonwealth governments of both political persuasions. Apart from the advantages of avoiding federal limitations on legislative power, it also avoids both Houses of the Commonwealth Parliament and presents a more than usually difficult target for judicial review.

Initially the practice was much less prevalent than it is now. Whenever the issue arose, however, in any significant context, there was uncertainty about the source of authority for it.

Comparisons occasionally were drawn with Canada and the United States, as the two most obviously comparable federations, in both of which a federal spending power was implied. But in both those federations, the power was implied to empower the central level of government to make grants to the provinces or states, in the absence of an equivalent to Australia's section 96. From that point of view, the inclusion in the *Constitution* of an express power to spend through the States operated against an implied power to spend in ways that could not be supported by legislation.

For a while, nevertheless, it was assumed that Commonwealth spending depended on the meaning of sections in the *Constitution* requiring parliamentary appropriation 'for the purposes of the Commonwealth'. There was disagreement over whether these purposes could be determined by the Parliament of the day or were circumscribed by constitutional limits. This debate intersected with academic writing encouraging the view that for the purposes of contract and spending the executive branch of government was the equivalent of an ordinary person. On this view, because contract and spending were consensual, they should not be subject to constitutional, including federal, constraints.

The source and scope of Commonwealth power to spend were challenged during the heady days of the Whitlam federal government: a government with an ambitious social agenda across areas of both Commonwealth and State authority, but a poor relationship with many of the States. One initiative was the Australian Assistance Plan: a plan to provide funds to 'Regional Councils for Social Development' across the country.

The validity of the plan was challenged by Victoria in 1975.[3] The *AAP Case* was one of those rare High Court of Australia decisions in which the plaintiff lost but made

advances in the doctrinal war. The Court divided equally (3-3) on the merits. The seventh judge, Sir Ninian Stephen, holding the ring, held that the plaintiff State lacked standing. This was a conclusion with which the others disagreed, but it nevertheless prevented Sir Ninian from reaching the merits.

On close reading of the reasons of the various judges, nevertheless, the doctrinal ground was shifting. The clearest indication of the change lay in the reasons of Mason J, which subsequently became the most influential. Appropriation was a process internal to the Commonwealth level of government; necessary, but not a source of a power to spend. The source of authority to spend and to contract was the executive power in section 61 of the *Constitution*. The executive power was limited; not only, obviously, by considerations of separation of power but also by the federal character of the *Constitution*, including the legislative division of powers. Even allowing for some flexibility in the 'federal' scope of the executive power, through the addition of a 'nationhood' component, the AAP scheme was beyond the pale.

Judicial challenges to government spending are unusual. Recipients have standing but are unlikely to object. The standing of third parties may be uncertain, as the *AAP Case* made clear. There was no early judicial follow-up to the decision in the *AAP Case*, to clarify its meaning. In these circumstances, the odd outcome led to divergent understandings across Australia. I can attest that students at Melbourne Law School were taught for the next 30 years that the Commonwealth power to spend was limited. In Commonwealth circles, however, the case seems to have been understood as something of a green light, requiring less attention to be paid to constitutional constraints.

And so matters stood until the end of the first decade of the 21st century when another three spending cases came before the High Court. The first was a fallout of the global financial crisis in a decision called *Pape*, which I will not canvass here except to note that it helped to lay the foundations for the others.[4] Both the remaining two cases dealt with a challenge to the School Chaplains' program. This program funded chaplains in schools across Australia, through contractual arrangements with participating schools. Some States had similar programs. The Commonwealth program was entirely dependent on executive action. It operated pursuant to executive guidelines, which were detailed and frequently changed. The program was challenged by Mr Williams, a parent of children at one of the schools. His standing was accepted by the Court or, at least, assumed.

In the first *Williams* case a majority of the High Court held that the contracts were invalid because they were not supported by the Commonwealth's executive power.[5] In other words, the High Court by this time had adopted the view of Mason J in the *AAP Case* that the source of the Commonwealth power to spend is the executive power of the Commonwealth. The school chaplains program was invalid because it needed the support of legislation. The flaw in the scheme, therefore, was linked to considerations of separation of powers. The analogy between the executive government and 'ordinary' people was repudiated. It was not necessary for the court in the first *Williams* case to consider the obvious potential for other flaws, derived from federalism, which might also have affected the validity of the scheme.

It was evident from this decision that there is no general, inherent, Commonwealth executive power to contract and spend. Some contracts can be made without supporting legislation. The scope of these is unclear, but they are likely to

include contracts made in the ordinary course of administration, and so attributable to section 64 of the *Constitution*. While the reasoning of the Justices varied, all drew on the structure of the *Constitution*, which included federalism and parliamentary democracy, in construing the meaning of the Commonwealth's executive power. The dependence of the reasoning of the court on the context of the *Constitution* makes it hard to predict with certainty whether State executive power is similarly limited (although my best guess is that it will prove to be).

As the hearing in the first *Williams* case progressed and the possibility of an adverse decision appeared to increase, the Commonwealth took steps to ascertain how many other spending programs might be at risk. The final tally was around 400, which may or may not have been complete. In the immediate aftermath of the decision in *Williams,* legislation hastily passed through Parliament provided a statutory basis for all existing programs in an unusual manner that gave them the status of delegated legislative instruments. The legislation also allowed for future spending programs to be put in place through delegated legislation. Political rhetoric at the time claimed that this was a temporary, stop-gap measure. In effect, however, it is still in place.[6]

The School Chaplains scheme, now with a form of delegated legislative underpinning, was challenged again by the indefatigable Mr Williams in the case of *Williams No. 2*.[7] And once again, the challenge succeeded. The Court stuck to its guns in relation to the scope of inherent executive power. But the real issue now was not separation of powers but the validity of the supporting legislation. The regulation that underpinned the School Chaplains program was oddly drafted and its purport not entirely clear. But at least it provided the Court with a text, which could be measured against the yardsticks that the

constitutional heads of legislative power provide. The Court found the regulation wanting, in the sense that it was not supported by any head of legislative power. Both benefits to students and the trading corporations power were rejected as possibilities. The case illustrates well how an understanding of the executive power that requires legislation for contracts of this kind serves to reinforce the federalism limits in the *Constitution*, as well as enhancing accountability to the Parliament. Direct action having failed, the decisions in these cases forced the Commonwealth back to section 96, requiring negotiation with the States, if it wanted to continue with the program.

I welcomed the *Williams* decisions (and I was not alone), as strengthening federalism and democracy, whether considered as values in their own right or as a compound conception of federal democracy. In a sense the decisions are timeless. But they are particularly important at this time. Current practice in the delivery of public policy relies extensively on public contracts for a range of purposes with contemporary and intergenerational significance: the performance of public services; very large-scale infrastructure and other projects; the sale of public assets. Australia is by no means the only country following these trends or grappling with the consequential issues. It is, however, grappling with them in the distinctive context of Australian constitutional federal democracy, fuelled by the fiscal imbalance. Elsewhere, there is burgeoning debate about suitable institutional mechanisms for public spending and public contracts that serve the public interest without undermining the fabric of the constitutional system. The *Williams* decisions provide the opportunity to have that debate here too.

So far, the opportunity has not been taken, although I do not despair. It must surely happen in due course, if only for reasons of budgetary prudence. Current Commonwealth spending practices raise obvious problems from the standpoint of fiscal management. No opportunity for prioritization. No attempt to fit isolated incidents of Commonwealth largesse with existing, developed State programs.

Meanwhile, however, the story continues. Regulations to underpin executive spending continue to be made. It is impossible to tell whether they are made for all new programs that the outcomes in *Williams* place at risk. The relevant Senate Standing Committee has insisted that the explanatory memorandum that accompanies new 'spending' regulations identify the head of power that supports each of them. The typical response, my cursory research suggests, is the 'nationhood' power; almost certainly a slender reed, if and when another of these programs reaches a court.

In the absence of a challenge, political practice is hard to shift. Those alive to these issues watched aghast during the last Commonwealth election campaign as candidates from both sides of politics promised goodies from football fields to car parks that are almost certainly beyond Commonwealth power, unless achieved through grants to the States. The sports grants affair raised the problem to a new level, with spending promises that were not only unsupported and unsupportable by legislation but were actually contrary to an existing Act.

To return to the connection with which I began. Alfred Deakin anticipated Commonwealth financial hegemony. He could not have foreseen these developments, however. They have implications for the effectiveness and integrity of government at the Commonwealth level. I like to think he would be concerned as well.

Endnotes

1 *New South Wales v Commonwealth (Surplus Revenue case)* (1908) 7 CLR 179

2 Alfred Deakin, *Federated Australia* (1968).

3 *Victoria v Commonwealth (AAP case)* (1975) 134 CLR 338.

4 *Pape v Commissioner of Taxation* (2009) 238 CLR 1.

5 *Williams v Commonwealth* (2012) 248 CLR 156.

6 See now the *Financial Framework (Supplementary Powers) Act* 1997 (Cth), s 32B.

7 *Williams v Commonwealth (No 2)* (2014) 253 CLR 416.