A UNIQUE FEDERAL INSTITUTION.

I. Introduction.

No federal institution in Australia has attracted quite the same degree of attention abroad as the Loan Council. The Rowell-Sirois Commission, the Groves Committee on Federal-State Fiscal Relations in the United States, the Rance (Caribbean Federation) Committee, the Central African Federation Conference, the Hicks-Phillipson Commission on Revenue Allocation in Nigeria, and the Indian Constituent Assembly have each in turn drawn on the experience of this body. And justly; for if Australia has made a unique contribution to federal finance it lies in its harmonisation of public borrowing by an institutional device which offers a solution for a host of related federal problems—the co-ordination of public investment, economic planning, tax conflicts, and so on.[1] In Australia, the full implications of this body are still in doubt. What is clear, however, is that in the Council's two primary elements of *co-operation* and *compulsion* Australian federalism finds its most symbolic expression. For in its origin and practice, the Council reflects the co-operative impetus of inter-governmental relations in Australia since the very conception of the federal movement. And in its compulsive force, it typifies the most direct consequences of political and fiscal centralisation in the Commonwealth. How far these two facets of the Council are compatible or incompatible in a federal system, however, is not to be answered by reference to some doctrinal notion of "federalism." It is not in the nature of political institutions to grow according to some archetypal pattern of development. Their growth is organic and their interpretation must take place in the context of their own special historical experience. In this article we hope to make some slight contribution to the understanding of this "unique institution" by an examination of its (a) origin; (b) structure; (c) procedure; (d) powers; and (e) implications.

II. The Origin of the Council.

One of the central features of Australian public finance towards the end of the 19th century was the large-scale expenditure of loan funds on public works—chiefly railways, water supply, roads, bridges,

[1] J. A. Maxwell, *The Recent History of the Australian Loan Council*, (1940) 6 Canadian Journal of Economics and Political Science, 22.

telegraphic services, harbours, and other public undertakings. This characteristic may be attributed to two related factors; first, the recognition by every colonial government that the major responsibility for development rested with the State; and secondly, the readiness of British investors to pour capital into Australian public undertakings.[2] A word of explanation will be useful. It has been fashionable to attribute the assumption of many activities which in other countries such as Great Britain or the United States had been left to the initiative of private enterprise to some "collectivist" purpose on the part of governmental activity in Australia. Such an explanation, however, is too suggestive of some doctrinaire ideology in the early growth of the Australian community. The state development of the public domain in Australia was due more to the pressure of "environmental" factors than to any coherent or consistent "idea" of the role of government in society. From the very beginning of Australian colonisation it was eminently clear that if this vast area of land with its natural perils of light rainfall, uncertain wealth, and minute population was to prosper, the development of the basic public utilities, more especially communication, was imperative. At the outset, the very conditions of penal settlement forced the initial responsibility for these tasks on the colonial governors; and from them a tradition of state development, born of necessity, maintained itself by the pressing needs of an expanding community long after the primitive "paternalism" of early settlement had come to an end. Private enterprise might have challenged this responsibility. At no time, however, did British or Australian capital make any serious attempt to intrude on this sector of public expenditure; for at first the hazards were too great, and the fields of alternative investment (for example, wool) too attractive; and then later in the century, when the six colonies had become reasonable investment "risks", government monopoly of the major public utilities was too firmly entrenched to be disturbed.

Given this role of government in Australia it is, nevertheless, very doubtful whether the public debt would have reached anything like its vast size had the rate of development been conditioned by the availability of internal capital. Until the middle of the 19th century the Australian colonies chiefly relied on customs revenue to finance their public works programmes. Borrowing was negligible. But with the grant of self-government and the wave of immigration which followed the discovery of gold, with the progress of land

2 See generally T. A. Coghlan, The Seven Colonies of Australasia, 797 *et seq.*

settlement and urbanisation, the need for public works multiplied rapidly. The supply of local capital was incapable of satisfying the demand, and the colonies therefore turned to London. At first their operations on the English market were fairly restrained. As Coghlan notes, there was considerable caution in the selection of works,[3] and in 1861, ten years after the first Australian loan was floated in London, the total indebtedness of the six colonies was no more than some eleven million pounds. Such moderation, however, was short-lived. The increasing eagerness of English capital to finance Australian developmental loans provided an irresistible temptation to the colonial governments; and from 1871 until the very eve of federation, the six colonies, encouraged by the cheapness of the English capital market, plunged into an orgy of expenditure.[4] In the space of some twenty years, the Australian public debt rose from 11 to 195 million pounds, a figure which Coghlan could describe in no other words than "astonishing."[5]

No less striking than the volume of Australian loans, however, was the "chaotic" state of the public debt itself. Borrowing was almost completely unco-ordinated and—frequently—competitive. Coghlan has left us an incisive comment on the credit operations of this period: "No combined action is taken to regulate the raising of loans, each colony acting according to the exigencies of its government, regardless of the financial conditions of its neighbours. The placing of a loan on the London market, especially if it be for a large amount, generally results in an all round fall in the prices of Australasian stocks, and subsequent issues of other colonies are placed at a disadvantage if the market is approached before it has recovered its tone; *in fact the colonies have in this respect all the evils of disintegration and all the liabilities of federation, without any of the advantages which federation would give.*"

Federation, however, brought only the promise of a remedy, no more. The principle of consolidating the debts of the six colonies into a single Australian stock was not in serious dispute. Indeed the belief that a substantial saving would accrue to the States through the transfer of their debts to the Commonwealth formed a strong electoral inducement to federation.[6] In the final Convention, how-

[3] T. A. Coghlan, Labour and Industry in Australia, III, 1419.
[4] T. A. Coghlan, *op. cit.*, 1405-1424.
[5] T. A. Coghlan, Seven Colonies of Australasia, 797.
[6] *Convention Debates* (Melbourne, 1898), II, 1641:— " . . . whatever sentimental advantages there may be about federation, whatever advantages—and there are many—to trade and commerce there will be connected

ever, an immediate transfer of the States' debts was rejected. Instead the Constitution simply vested the Commonwealth with an optional power to assume the pre-federation debts of the States—the time, method, and conditions of transfer were left to its sole discretion.

The reasons for this arrangement were fourfold. In the first place, the financial settlement had proved the most intractable problem of the Conventions. The discussions ranged over a number of alternative methods of distributing revenue between the needs of the Commonwealth and the States. The search for the "permanent" formula, however, proved fruitless. What emerged instead from the tortuous debates was the growing conviction that a final settlement—however desirable to some—was an impossibility. The future needs of the Commonwealth and the States were in-

with federation, all through the sittings of our Convention, in the three places where we have sat, there has been running frequently this note—"What can we tell the electors whom we represent they will receive as actual profit from the proposed federation?" Now, to my mind, the only cash dividend which federation can pay . . . the only cash arrangement we can use to our constituents in recommending them to adopt federation will be the profit arising from any possible conversion of our loans. That is taken for granted by practically all those who, in the press, have written on federation with any financial knowledge and experience; that is the only argument I have heard used, even in this Convention, in favour, from that point of view, of the federation we are striving to frame" [the Hon. F. W. Holder (South Australia)]. Clearly federation appealed to the pocket as well as to the soul. It was popularly argued, for example, that by the substitution of a superior federal credit for the credit of each state, a saving of 1% would be realised; and hence on a total public debt of some 200 million pounds at the time of federation the saving of 2 million pounds per annum would more than compensate for the cost of federation—then somewhat sublimely fixed at £200,000 per annum. It is an interesting reflection of the "enthusiasm" (or innocence) of the time that this estimate of the "cost" of federation should have obtained such wide currency. Coghlan's acid comment on the expectant "cost" of federation is sufficient:— "The additional expenditure that Federation would impose on the Australian communities was estimated by the financial committee of the Convention at £300,000. This was a ridiculously low estimate. It took no account of the expenditure required to bring the defence cost of the country to a state of efficiency, nor of the probable cost of old age pensions and other services which it was anticipated would be provided by the Commonwealth. There was nothing in the Constitution itself which encouraged the expectation of so restricted an expenditure. There was no limit placed upon the expenditure which Parliament might sanction, nor the method by which revenue might be raised . . . " (Labour and Industry in Australia, IV, 2358). Note the recurrence of this form of "popular" incentive to federation in the Report of the Rance Committee on the proposed federation of the West Indies.

determinable; and at best the arrangement could only be tentative.[7] This same hesitancy, the same practical regard for the uncertainty of the future underlay the rejection of an immediate transfer of State debts. The full implications of this transaction were no less uncertain. It touched the future of the States' capital assets. And, for most, it was inextricable from the overall financial settlement. Clearly, if caution dictated a tentative solution in one, it was no less important for the other. In the second place, the majority of federalists were insistent on framing the power to consolidate the States' debts in terms which would afford the Commonwealth complete freedom to choose the right moment for the transfer.[8] They believed that in the very nature of the operation, "timing" was a paramount consideration; and to deprive the Commonwealth of this discretion might deny to the States the full benefits of the transfer. Thirdly, New South Wales—the sole "free-trade" State—set itself against any suggestion of a compulsory transfer. Throughout the debate its arguments were dominated by one factor—the deep-rooted dislike of any step which might commit the Commonwealth to a high tariff.[9] Finally, one other factor dictated an optional transfer. It is clear that if the federalisation of the States' debts was generally desired, not all were certain of its effect on future borrowing. For some, transfer of their debts automatically involved the centralisation of borrowing; for others, the two operations were distinct and separate. For all, however, it was patently clear that to link the two together at this stage would completely abort any hope of incorporating a power of transfer in the Constitution. Here too, therefore, as in so

7 In 1901, the Australian constitution embodied a financial settlement which was chiefly concerned with two objects:— return of a fixed share of the Commonwealth revenue from customs and excise to the States (sec. 87), and the assurance of financial aid to "necessitous" States (sec. 96). On its face, it appears to have been an act of extraordinary faith in the Commonwealth, or political myopia on the part of the States, to commit their financial future so unreservedly into the hands of the federal government. In fact it was neither. The financial provisions, although a last-minute compromise, represented an act of considerable wisdom. It rejected the possibility of a permanent fiscal settlement; it accepted the necessity for flexibility in the financial relations of the Commonwealth and State governments; and it reposed its "faith" in "political" restraints on federal power rather than constitutional safeguards [See, for example, Holder in *Convention Debates* (Melbourne, 1898), II, 1599 *et seq.*].

8 See *Convention Debates* (Adelaide, 1897), 1088, and (Melbourne, 1898), II, 1606.

9 See Quick & Garran, Annotated Constitution of the Australian Commonwealth, 923-924.

many other problems, the federalists left the matter to the future.[10]

For twenty-seven years the problem of State debts remained unresolved, and for almost all that time the pre-federation pattern of independent borrowing continued despite intensive efforts to find a solution. The movement to co-ordinate public borrowing, however, began as early as 1903, and indirectly emerged from the States' pressure on the Commonwealth to assume their public debts as part of a general financial settlement.[11] The basic attitudes on the future of public borrowing were struck at the first Australian Treasurers' Conference (1904) and, with few variations, were largely maintained by each government for the next twenty years, irrespective of the change of personnel or of their political complexion.

In the Commonwealth view, the transfer of State debts and the co-ordination of public borrowing were inseparable. To secure the benefits of a consolidated public debt, some provision for the regulation of future borrowing was essential; otherwise the whole purpose of consolidation would be lost if the States were left free to build a further mass of unco-ordinated debts. Every federal proposal for the assumption of the States' debts, therefore, was in-

10 *Convention Debates* (Sydney, 1891), 839-840:— Mr. W. McMillan (New South Wales) speaking against immediate transfer: " . . . I thoroughly believe in the consolidation of the debts of the colonies ultimately; but I think we have just reached that stage of our proceedings when we are liable to go too far . . . there are a great many consequences arising out of such a course as is proposed. In the first place, if you take over all the debts you must regulate the borrowing in the future, and with colonies under such different conditions it seems to me that if we now enter upon this dangerous ground we shall open for ourselves a battery of opposition on the part of some of the colonies which it will be absolutely impossible to silence." Mr. G. R. Dibbs (New South Wales), (supporting McMillan's strictures on a compulsory transfer): "If we agree to this clause, we may as well procure a hundredweight of dynamite and blow the whole thing up." Mr. McMillan: "That would be a veritable bomb-shell. If we simply give, as this bill gives, to the federal parliament the right to negotiate with the other parliaments—and I believe a great deal will be done in future by negotiation, and that a great deal will be undertaken by negotiation that is not provided for in the four corners of this constitution—and if we imply by this clause that such a thing may be a benefit in future to all the parties concerned, we shall go as far as we possibly can . . . the project is surrounded with enormous difficulty. It must be a matter for the future."

11 The view has been expressed that it was not until the 1920's that the need for some regulation of public borrowing became recognised. This view is only tenable if 1920 is treated as a critical point in the development of the Australian public debt. Otherwise it ignores the negotiations which began with the first Australian Treasurers' Conference in 1904. See, for example, N. Cowper, *The Financial Agreement*, in Studies in the Australian Constitution (1933), 119, and especially at 143 *et seq.*

variably linked to a plan for the control of future borrowing.[12]

The States' view was no less clear, and expressed itself in one common syllogism. In the general distribution of power under the Constitution, two broad functions, land settlement and development, remained the major responsibilities of the States; the performance of these functions was vitally linked to continued public borrowing; hence to submit their loan requirements to any form of federal regulation was tantamount to the federal control of State developmental policy. Until 1927, every Commonwealth proposal for the permanent co-ordination of public borrowing broke down on this argument.

Around this central theme, furthermore, revolved an admixture of particularist attitudes. In the first place, the importance of public borrowing largely varied with the developmental needs of each State. For every State, public loans had assumed a dominant role in its economy;[13] but for the large, sparsely populated and poorer States, it had become an even greater precondition of their development. However enticing the attractions of consolidation, restrictions on borrowing were even more repugnant to them than to any of the other States. For them, too, the preponderant influence of the two wealthy States—New South Wales and Victoria—in the Commonwealth parliament further aggravated their fear of federal control.[14] On the other hand both New South Wales and Victoria, much as they protested their desire to see the consolidation of the States' public debts, persistently argued that they could always borrow as cheaply, alone, as the Commonwealth, if not more cheaply. The financial press supported this belief for some time; and even Coghlan, who argued so cogently for consolidation, assumed that the potential superiority of Commonwealth credit *was incapable of immediate*

12 Note Coghlan, *Commonwealth Parliamentary Papers*, (1906), II, 1015. Coghlan warned the Commonwealth that "if the transfer of the existing obligations of the States to the Commonwealth were coupled with the right of the States to continue borrowing on the London market", the result would be disastrous. See also *The Economist* of 25th April 1908, at 885; Reid, *Convention Debates* (Adelaide, 1897), 1088; and McMillan, *Convention Debates* (Sydney, 1891), 406.

13 See B. P. Adarkar, The Principles and Problems of Federal Finance, 150.

14 See *The Economist* of 9th April 1904, at 606:— "It would never do for the Commonwealth Parliament, under the preponderating influence of the two larger States, as regards population, to be able to veto the financial proposals of the smaller States. But the State Treasurers recognised that when several States are desirous of borrowing an amicable arrangement as to dates of issue should be entered into."

realisation.[15] Again the argument of almost every State reflected an occasional echo of party conflict. It is most difficult to give this factor anything but the crudest weighting in relation to the common desire to remain completely free of federal control. It is clear, however, that the resistance of non-labour States to the centralisation of borrowing was partly stimulated by the fear that a federal Labour government might restrict, if not positively discourage, British investvestment.[16] And conversely, Labour States, especially New South Wales, were reluctant to risk the possible restraint of non-Labour federal governments.

Out of this web of issues and motives, the co-ordination of public borrowing in Australia presented two main problems:— First, to reconcile the interests of the Commonwealth and State governments; and secondly, to rid each State of the fear of interference, either from the Commonwealth or from other States, with its developmental policy.

For our purpose there is little need to trace the history of the negotiations—or to analyse the range of proposals and counter-proposals—which led to the establishment of the Australian Loan

15 See for example, Waddell (Treasurer of New South Wales), *Commonwealth Parliamentary Papers* (1904), II, 1690:— "If it were quite clear that the Commonwealth Government could borrow much cheaper . . . the question would be worthy of our consideration. If that fact were demonstrated beyond doubt . . . the position would be altered; but it has not been demonstrated." See also *The Economist* of 25th April 1908, at 885, for the expression of a similar view; also (1905) 29 Australasian Insurance and Banking Record, 77. Both T. A. Coghlan and Robert Harper, who strongly advocated the consolidation of State debts, agreed that the virtues of a single Commonwealth credit would not be realised for some time. See Coghlan, *Commonwealth Parliamentary Papers* (1906), II, 1014; and Robert Harper, Financial Problems of the Constitution of the Commonwealth of Australia, 1024.

16 The financial press in both the United Kingdom and Australia especially expressed this view. See for example *The Economist* of 27th August 1910, at 434 (Melbourne Correspondent):— "Australia is so vast a country, and the demands for development of the several States so diverse in their character, that it is only reasonable that the borrowings should be left to the State Governments, who would be better able to form a judgment than *a junta of Labour members sitting in Melbourne, who know so little of the country, excepting as a fine field for the exercise of the arts of the agitator*" (italics added). And (1911) 35 Australasian Insurance and Banking Record, 9:— "It is thought that the Commonwealth would be able to borrow on better terms than the States . . . for the reasons frequently expressed in these columns, the advantage under the most favorable circumstances would be slight. *There is the additional consideration that the Labour party which is in power has shown itself extremely inimical to the interests of British lenders and investors in Australia* . . . the States will act very unwisely if under existing conditions they volun-

Council.[17] The factors which ultimately brought the Commonwealth and the States into agreement to regulate public borrowing are of more interest. Briefly they were the impact of the First World War on Australian finance; the growth of Commonwealth fiscal power; the deterioration of State finance; the condition of Australian public borrowing in the 20's; the influence of the voluntary Loan Council, and the intense pressure exerted by the Commonwealth to secure a comprehensive financial settlement with the States.

In all, these factors span a short period of less than thirteen years; in retrospect, however, it is difficult to resist the view that without the catalytic impact of war the Australian Loan Council

tarily surrender the control of the debts to the Commonwealth . . . under the constitution the States cannot be compelled to surrender their borrowing powers and it is to be hoped that they will never consent to do so.'' Note the interesting view of *The Economist* of 27th June 1903, at 1133-4 (Melbourne Correspondent)— '' . . . *the transference of the State debts to the Commonwealth should be almost the last surrender to be made by the States, seeing that it is as yet not impossible that Federation may break down*'' (italics added). See also (1905) 29 Australasian Insurance and Banking Record, 77; and T. A. Coghlan, *Commonwealth Parliamentary Papers* (1906), II, 1013.

17 For a detailed history of the proposals and negotiations, see *Premiers' Conference* (1903) and *Premiers' Conference* (1904), and the proposals made by William Knox to the House of Representatives in 1904. In many respects Knox's proposal must be regarded as the precursor of the Australian Loan Council in the sense that he was the first to suggest a solution on ''institutional'' lines. He proposed the establishment of a *Council of Finances*, a ''highly ,competent and representative central authority possessing the confidence of the Commonwealth and the States'', to conduct the loan operations of the Federal and State governments: (1904) 23 Commonwealth Parliamentary Debates, 6481-6491. See also *Premiers' Conference* (1907)—Sir John Forrest's proposal; *Premiers' Conference* (1908)—Sir William Lyne's Council of Finance; *Premiers' Conference* (1914); Cambridge History of the British Empire, VII (Part I: Australia), 588-592, which describes the war-time (1914-18) borrowing arrangements between the Commonwealth and the States; and the Report of the Executive Officer to the Premiers' Conference (May 1916), 100. For details of the war-time arrangements see (1915) 39 Australasian Insurance and Banking Record, 1009; *Premiers' Conference* (January 1917), 76, and *Premiers' Conference* (1916), 2; *Conference of Commonwealth and State Ministers* (January 1919), 13; *Premiers' Conference* (May 1920); *Conference of Commonwealth and State Ministers* (1923), 42; and *Premiers' Conference* (June 1927), especially at 13 and 21. See also *The Economist* and *The Statist* of this period, and the following issues of the *Australasian Insurance and Banking Record* (the figures in brackets indicating page numbers):— February 1905 (77), 20th May 1908 (355, 357), 29th April 1914 (280-281), 21st May 1917 (365), 21st February 1924 (96-97, 138-139), 21st July 1925 (519-520), 21st June 1926 (444), 21st January 1927 (8), 21st May 1927 (358), 21st June 1927 (456-457), and December 1927 (1041).

may have remained an aspiration, no more. On the eve of the First World War, negotiations had reached a complete impasse. A large variety of proposals had been exhausted; and there seemed little, if any, early prospect of bridging the outstanding differences between the Commonwealth and State governments. Then the outbreak of hostilities in Europe introduced two fundamental changes in Australian finance; first, at the request of the British government, credit operations in London for other than military purposes ceased; and next, the federal government was compelled to make unprecedented demands both in London and upon the Australian loan market. Almost immediately the whole situation was transformed. In the first place, the Commonwealth was anxious to limit competition as much as possible; and secondly, it became imperative to make some provision for the States, already committed to a heavy developmental programme. The result was a series of temporary agreements (renewed throughout the war) between the Commonwealth and the States to divert a fixed portion of the federal loans to the States, and in return the States undertook not to borrow on their own account except for local operations and renewals.[18]

This experimental trial in loan co-operation—though limited in scope—largely satisfied the war-time needs of the Commonwealth; and shortly after the armistice, the federal government took steps to renew these arrangements. Its urgency was understandable. The Commonwealth had emerged from the conflict burdened with a massive war debt. Together with the States it faced a serious problem of reconstruction. Soldier settlement, repatriation, and an accumulated programme of State public works pointed to an early resumption of large-scale borrowing by each government. Added to this, the imminence of extensive Commonwealth and State renewals, plus the abnormal condition of overseas loan markets, argued strongly for some understanding between the federal and State governments.[19]

With the end of the war, however, the stimulus of the national emergency was dissipated, and the underlying compulsion of the war-time agreements removed. The first peace-time discussions im-

[18] See Fisher's budget statement in which the circumstances of the loan are set out in detail: (1914) 75 Commonwealth Parliamentary Debates, 1340-1341. Note L. F. Giblin's evidence before the Rowell-Sirois Commission, Appendix H, 26; K. O. Warner, An Introduction to some Problems of Australian Federalism (1933), 147; and (1915) 39 Australasian Insurance and Banking Record, 1099.

[19] See text of federal memorandum submitted to the States prior to the Conference of Commonwealth and State Ministers (appended to the *Report of the Conference* (1919), 13).

mediately revived the *motif* of the pre-war negotiations; fear of central control, desire for unrestricted borrowing, and once more an assertion by the senior States that the superiority of the Commonwealth credit was an illusion.[20] The war-time arrangements were therefore abandoned, and the States reverted to independent borrowing. From 1919 until 1923 Australian borrowing was reminiscent of the prodigality of the late 80's and 90's. The States again indulged in a welter of loan expenditure. The public debt rose precipitately. The era of "artificial prosperity" induced by heavy governmental expenditure, together with competitive borrowing in London in the face of heavy losses on soldier settlement projects, aroused growing concern for Australian credit. By 1923, the need for some reduction and co-ordination of public borrowing became a critical national problem.[21]

The Premiers' Conference, convened by the Commonwealth in 1923 to discuss this situation, was an historic meeting. The State governments were substantially of the same political complexion, and even of the same personnel who had three years earlier rejected a further Commonwealth offer to co-ordinate borrowing on the lines of the war-time agreements. On this occasion, however, a Commonwealth proposal to end "undue competition" by establishing a "Loan Council consisting of the Treasurer of the Commonwealth, and the Treasurers of the States" (a) to determine "the *order* in which the Commonwealth, the States and the various public bodies created by the State legislatures should come upon the market *within Australia*", and (b) "to advise each Treasurer as to the rate of interest and the other terms upon which local loans should be floated", was accepted by all States. *Why?* Unfortunately there is no adequate record of the discussions.[22] Nevertheless a number of reasons may be suggested. In the first place, the condition of Australian borrowing was obviously an important contributory factor. Possibly, too, the political homogeneity of the Conference—a rare event—and the removal of the strident and choleric war-time Prime Minister (W. M. Hughes) from the federal leadership may have introduced some element of personal harmony. What stands out foremost from the discussions, however,

20 *Conference of Commonwealth and State Ministers* (1919), 39, 47, and 54.

21 See federal memorandum submitted to the *Conference of Commonwealth and State Ministers* (1923), 42.

22 The material discussions were carried out by the Premiers prior to the main conference, and in the absence of the verbatim discussions it is difficult to examine the arguments which led to this agreement. The record of the main conference provides only a slight indication: see *Conference of Commonwealth and State Ministers* (1923), 42-45.

was the common feeling that little "harm" could come from a purely *voluntary* Loan Council.[23] Until 1923 every Commonwealth proposal—however restrained—rested on the assumption that borrowing should be conducted through a central agency. In 1923 even this condition was abandoned. By contrast this proposal was modest in the extreme—to eliminate "undue competition and clashing" by agreeing on the order, rate of interest, and general terms of the loan—not to centralise (or restrict the volume of) State borrowing.[24] It was initially understood that each State would remain responsible for its own flotations. The Council was to function solely as an informal arrangement between the federal and State Treasurers. It had no executive authority; its recommendations were subject to the approval of each government; and it imposed no greater restraint than its members chose to accept.

This policy of gradualism was a brilliant manoeuvre by the Bruce-Page coalition and reaped considerable profit. In five years, the operation of the voluntary Loan Council—despite the temporary withdrawal of New South Wales in 1925—provided invaluable experience of co-operative borrowing. At first, its activities were restricted to the barest limits of co-operation. But with each meeting and with each successful flotation, as confidence grew in its operations, so the scope of its activities was extended, and the resistance to centralised borrowing declined.[25] Perhaps the most convincing evidence of its prestige and the understanding achieved in this brief period of concerted action, however, is revealed in the dramatic events which led to the Financial Agreement of 1927.

We need not trace the general history of federal-State financial relations here. Sufficient to say that the establishment of the voluntary

23 *Ibid.*, at 45 (Sir James Mitchell).

24 *Ibid.*, at 44, (S. M. Bruce):— "I should like to make it very clear that the powers of this Council would be very limited. We are not endeavouring to achieve what we have heard a good deal about from time to time; that is, some means by which one authority should borrow for the whole of the Commonwealth. That proposal has been examined closely, and we have come to the conclusion that at the moment . . . it is impracticable to provide that one authority shall borrow sufficient to meet the requirements of the Commonwealth."

25 See Bruce, *Premiers' Conference* (June 1927), 13 and Lyons, 21. For details of the voluntary council in this period, see a valuable note by H. J. Exley on *The Australian Loan Council* in (1926) 2 Economic Record (Melbourne University Press), 84-87. See also Australasian Insurance and Banking Record of 21st February 1924 (96-97, 138-139), 21st July 1925 (519-520), June 1926 (444), 21st January 1927 (8), 21st May 1927 (358), 21st June 1927 (456-457), and 21st December 1927 (1041).

Loan Council in the 20's marked the beginning of determined federal efforts to reach a comprehensive financial settlement with the States.[26] Briefly, the moribund condition of State finance in the 20's reflected the combined effects of excessive borrowing, post-war disturbances, and the anomalous operation of the federal-State financial adjustments since 1901. The question of debts, always a major drain on State revenues—now, more than ever—dominated the budgetary problem of the States. By comparison the Commonwealth had acquired a position of unprecedented financial strength. Its fixed commitments were relatively small; and its revenue experienced all the benefits of an increasing volume of imports and an expanding protectionist policy. Clearly some adjustment was vital. In 1926, therefore, the federal government made a four-point proposal to the States; (a) to take over the entire public debts of the States; (b) to terminate *per capita* payments to the States and make a fixed annual contribution towards the payment of interest charges instead; (c) to make a substantial contribution to sinking funds; and (d) *to establish a representative Loan Council to manage the debts and future borrowing of the federal and State governments.*[27]

The equity of this scheme to rationalise Commonwealth-State financial relations need not detain us. From the outset the negotiations which culminated in the Financial Agreement were conducted in an atmosphere of great tension and bitterness. Commonwealth pressure was unremitting; and there is probably little doubt that the States were brought to the Financial Agreement "at the point of a gun." In all this episode, however, two things are often overlooked. In the first place, no matter how acrimonious this period or how strong the resistance to this financial scheme, the proposal to establish a permanent Loan Council provoked the least controversy. Indeed, in contrast with their former deep-rooted hostility to permanent regulation, each State, with the temporary exception of Western Australia and New South Wales, accepted the control of borrowing as an essential corollary to the consolidation of their public debts. And the reasons for this transformation? Of the large number, the principal reason lies in the States' experience of the voluntary Loan Council.[28] These comments are sufficiently explicit:[29]

26 The pattern of Commonwealth-State financial relations since federation has been adequately surveyed in the early reports of the Commonwealth Grants Commission, especially 1933, 1934, and 1935.

27 *Premiers' Conference* (June 1927), 3-7.

28 See (1944) 180 Commonwealth Parliamentary Debates, 2516 (Sir Earle Page).

29 *Premiers' Conference* (June 1927), 18, 20, 21.

"I cannot conceive of any Commonwealth government taking over the huge loan liability from the States without having some protection. I have not the slightest objection to the loan expenditure of my State being reviewed by what I regard as an independent tribunal" (Butler, South Australia).

"I can quite understand the objections which some representatives have to constitutional provision being made for . . . a Loan Council, thinking that the operation of such a body may be a disadvantage to the States; but it is my experience that there had been no antagonism between the States, or between the Commonwealth and State representatives. We should be guided by experience, and if Mr. Lang, who is hostile to the constitutional proposal, had become a member of the Council he would be of the same opinion" (Lyons, Tasmania).

But if these were not enough, then the remark of one of the two dissentients, "If I were sure that the proposed Council would work as smoothly as the one now in existence I would have no objection to offer" (Collier, Western Australia), is a compelling comment on the States' final conversion.

The second reason deserves no less emphasis. It is clear that if the broad terms of the financial settlement were "dictated" by the Commonwealth the final structure of the Loan Council emerged only after considerable discussion and agreement with the States on many of its vital terms. For example, the original draft of the Council submitted by the Commonwealth underwent at least three important amendments;[30] first, the crucial "formula" clause which provided for the allocation of the loans in the event of disagreement between the governments was altered to meet the objections of Mr. J. T. Lang of New South Wales;[31] secondly, provision was made to continue the States' practice of raising small loans within their own territory from such sources as local banks, public trust funds, and so on; and finally, provision was made to enable a State—with the unanimous approval of the Council—to borrow overseas on its own account.[32]

30 For the original draft, see *Premiers' Conference* (June 1927), 5; for the first amended draft as it emerged from committee, see 28-29; and for the final draft as embodied in the draft of the Financial Agreement, see *Premiers' Conference* (July 1927), 54-56.

31 Cf. original clause (f) in *Premiers' Conference* (June 1927), at 5 and amended clause (i) at 29.

32 See *Premiers' Conference* (July 1927), 55-56, and sec. 4, clauses (a) and (b). The clauses were inserted at the insistence of New South Wales. It is interesting to note, however, that on no occasion did this State, or for

III. The structure, functions, and scope of the Australian Loan Council.

The Australian Loan Council was formally established in 1929 as a statutory and constitutional body in pursuance of an amendment to the Constitution, sec. 105A, and legislative ratification of the Financial Agreement of 1927 by each of the seven parliaments.[33] Its structure, functions, and powers are derived in the first instance from the terms of the Financial Agreement itself; and its constitutional sanction through sec. 105A, which gives pre-eminent binding force to the terms of the Financial Agreement.

It has been suggested—and not without some undue alarm—that the effect of sec. 105A is to set any Financial Agreement "beyond the reach" of the normal process of constitutional amendment.[34] The proposition is a little startling and the arguments are

that matter any other State, avail itself of this opportunity to borrow independently abroad after the establishment of the Loan Council. Indeed, the possibility of securing the Council's unanimous approval to such a request seems sufficiently slender to make this "privilege" illusory.

33 *Commonwealth*—Financial Agreement Act (No. 5 of 1928), and Financial Agreement Validation Act (No. 4 of 1929). States: *New South Wales*— Financial Agreement Ratification Act (No. 14 of 1928); *Victoria*— Commonwealth and States Financial Agreement Act (No. 3554 of 1927), *Queensland*— Commonwealth and States Financial Agreement Ratification Act (No. 22 of 1927); *South Australia*— Financial Agreement Act (No. 1837 of 1927); *Western Australia*— Financial Agreement Act (No. 1 of 1928); and *Tasmania*— Financial Agreement Act (No. 97 of 1927). The original Financial Agreement between the Commonwealth and the States was made on 12th December 1927; the federal Constitution was subsequently altered by the insertion of sec. 105A (by Constitution Alteration (State Debts) 1928, which was approved by referendum on 17th November 1928 and, having been assented to on 13th February 1929, became Act No. 1 of 1929). The Commonwealth Parliament then passed the Financial Agreement Validation Act (No. 4 of 1929), similar legislation being passed by the States. The purpose of amending the Constitution (by the insertion of sec. 105A) was (a) to empower the Commonwealth to enter into financial agreements with the States; and (b) to give permanent and constitutional effect to any such agreements. The present consolidated Financial Agreement (1944) consists of two parts. The first part constitutes the Australian Loan Council, defining its structure, functions, and powers, and deals with the future borrowing of the Commonwealth and States. The second deals with the transfer of State debts, the payment of interest, sinking fund arrangements, the expenses of loan flotation, indemnification of the Commonwealth against all liabilities assumed on behalf of the States, and the maintenance of separate accounts by the Commonwealth for each State in regard to their debts, interest, etc. The agreement is fixed for 58 years. Technically, therefore, the Loan Council's authority ends in 1987.

34 See K. H. Bailey in *Studies in the Australian Constitution*, 48, and Sir Edward Mitchell, *What Every Australian Ought to Know* (1931), 68-73.

somewhat slender. However, if this view is correct, it is extremely important not to confuse this presumed difficulty with the clear right of the parties to vary or rescind the agreement at will (sec. 105A (4)). Of course, the task of securing unanimity in the Council and concerted action among the seven parliaments may well import an element of "rigidity" into this mode of amendment. But by comparison with the normal process of constitutional amendment, this method has proved almost the acme of flexibility. Since 1929, the Financial Agreement has been formally amended on four occasions,[35] while at least two of the most important changes effected in the Loan Council—the "gentlemen's agreement" to control the borrowing of local and semi-governmental authorities (1939), and the appointment of a Co-ordinator General of Works to the Council (1941)—were introduced informally.

The structure of the Loan Council is relatively simple. In broad outline it corresponds to the general pattern of inter-governmental consultative machinery in Australia. Like its political counterparts, the Premiers' Conference for example, it is a ministerial council representative of the Commonwealth and each State. Similarly, it resembles the procedure of the Conference in that its decisions are mainly formulated by discussion "around the table" between the Commonwealth and State representatives. But here its resemblance ends. Unlike the common pattern of consultative machinery it is distinguished by at least three *formal* characteristics; first, its composition is specifically defined; secondly, its decisions are final and binding on its members; thirdly, where the consultative councils must rely on compromise to settle their disputes, the Loan Council, failing compromise, may generally apply special voting arrangements, or resolve one major decision—the apportionment of loan funds—by an automatic formula.

35 The four amendments are (1) the Debt Conversion agreement—see (Commonwealth) Act No. 14 of 1931; (2) the second Debt Conversion Agreement—see (Commonwealth) Act No. 52 of 1931; (3) the Financial Agreement relating to Soldier Settlement Loans—see (Commonwealth) Act No. 26 of 1935; and (4) the Amending Agreement of 1944. As to the latter, see the following Acts: *Commonwealth*— Financial Agreement Act (No. 46 of 1944); *New South Wales*— Financial Agreement Act (No. 29 of 1944): *Victoria*— Commonwealth and States Financial Agreement Act (No. 5051 of 1944); *Queensland*— Commonwealth and States Financial Agreement Further Variation Act (No. 17 of 1944); *South Australia*— Amending Financial Agreement Act (No. 34 of 1944); *Western Australia*— Financial Agreement (Amendment) Act (No. 18 of 1944); and *Tasmania*— Financial Agreement (Variation) Act (No. 37 of 1944).

The Loan Council is composed of seven members, normally the Treasurers of the seven governments. The Financial Agreement specifically designates the Commonwealth Prime Minister and the Premier of each State as members of the Council. But since the chief political executives in Australia generally combine the dual office of Premier and Treasurer, the formal requirements of the Agreement are satisfied. Where the Premier attends, he attends as of right; and his tenure on the Council is coincident with his position as the chief political executive. Where the two offices are separate, however, the Premier is empowered to nominate an "appointee" who is almost invariably the Treasurer. The power of appointment is carefully defined to preserve the ministerial character of the Council. Departure from this rule is only permissible in "special circumstances" when the Premier may accredit "*some* other person" of non-ministerial rank to the Council. Presumably, under this exception, the Premier may appoint any member of Parliament or of the public service, or for that matter a private citizen.[36] In all cases of appointment, however, there is no fixed tenure on the Council; office is held only "during the pleasure" of the chief political executive of the Commonwealth or State governments.

The permanent chairman of the Council is the Commonwealth Prime Minister. This follows the practice of the Premiers' Conference, but is in contrast with the rotation of the office of chairman in such consultative bodies as the Australian Agricultural Council. The justification for the Prime Minister's role of *primus inter pares* is, of course, the predominant federal interest in the fiscal commitments of the Council. And on this ground, the explanation is probably decisive. Nevertheless, it is tempting to reflect how far personal relations in the Council might be improved—not to speak of gratifying the fiction of constitutional equality—if the practice of rotation were introduced into the Council. The loss of some administrative convenience would be negligible in comparison with the psychological gain.

[36] So far it appears that no appointee of non-ministerial rank has ever been accredited to the Council as a representative of any government. Clearly the emphasis on ministerial rank is understandable in view of the Council's function. Furthermore, the power to vote presumes that if a government is to be bound by the Council's decisions it will at least be represented by a member of its ministry. Note Mitchell, *op. cit.*, 11, who suggests that the provision for the appointment of non-ministers where special circumstances exist (e.g., financial depression) would enable the appointment of "men of successful experience in business and finance" to exercise the powers of the Loan Council.

The Loan Council is not obliged to meet at fixed intervals. The Financial Agreement vests the Council with complete discretion in regard to the "places, times, and notices of meetings." The Commonwealth is responsible for convening the Council. It may exercise this right "at any time"; but at the "request" of at least three States it *must* convene the Council. In this respect, therefore, it appears that the States enjoy a considerably stronger position as legal members of the Loan Council than as conventional members of the Premiers' Conference. In the current practice of the Premiers' Conference, for example, the Commonwealth is responsible for its organisation, and if it refuses to summon a conference the States cannot compel it to do so. At best, the States can organise a meeting independently with all the limitations which the absence of the Commonwealth implies. In regard to the Loan Council, however, the "request" of at least three States is sufficient to activate its machinery. The spectacle of April 1948, when a Federal Prime Minister rejected the request of three States to call a Premiers' Conference, is inconceivable in the Loan Council.

A meeting of the Loan Council is not impaired either by the absence of any member, or by any "vacancy" in its membership. A simple majority of the Council is sufficient to exercise its powers, though an absent member is entitled to appoint a deputy or to vote on any matter by letter or telegram. If a State, however, refuses to attend a meeting of the Council, or if a State "walks out" on its proceedings, or if a State is seized with the desire to reverse "traditional" fiscal practice by living on revenue alone, then, providing there is a quorum of four members, "a decision in which all the members for the time being . . . concur is a "unanimous decision" for all the purposes in which unanimity is necessary to the operation of the Loan Council." In short, a "Lang withdrawal" cannot abort the Council's activity.

The administrative machinery of the Council is remarkably small. It centres in two officers:— the Secretary of the Council and the Co-ordinator-General of Public Works. The normal administrative routine—minutes, correspondence, organisation of meetings, and so on—is the responsibility of the Secretary of the Council, an officer specially appointed by and accountable to the Council. The Council is free to select anyone for this post; but so far, for reasons of convenience, it has invariably appointed a Commonwealth Treasury Official. He remains a member of the Commonwealth Public Service, and the administrative cost of his office—together with secretarial assistance—is provided by the Commonwealth. The Co-ordinator-General of Public Works is a recent accession to the Council. Shortly

after the outbreak of war, in the primacy of Commonwealth defence needs, and the importance of reducing ordinary civil works to a minimum, the Loan Council agreed to appoint a Co-ordinator-General of Public Works[37] to review the composition of the individual works programmes of each State, to report on their economic and military significance, and to recommend the borrowing to be made by the Council. Originally, the Co-ordinator-General's Office was intended solely as a war-time measure. In 1946, however, the appointment was tacitly continued—surprisingly without protest from any member of the Council.

The Co-ordinator-General is a Commonwealth officer, and works in collaboration with the relevant officials of each State to present the Loan Council with a detailed statement of works proposed by every important governmental unit and department for each year. In this collaboration of Commonwealth and State officials, it is tempting to see the outlines of an informal "secretariat" to the Loan Council. The short answer is that there is no secretariat attached to the Council, and the activities of the Co-ordinator-General's Office form no more than the barest semblance to the real functions of such an organisation. Periodic efforts to create a Loan Council secretariat have been made at various times, but without success. The reasons are not altogether clear. It appears that the Commonwealth has been its warmest protagonist, while most of the States have been generally suspicious of its implications. It was suggested to the writer by a federal official—perhaps in jest—that State disapproval sprang from the fear that the weight of *expertise* might prove embarrassing to a State Premier determined to carry out a project more in the thought of electoral "bread and games" than sound public finance. "Log-rolling", however, is not endemic to the States alone; nor is *expertise* a Commonwealth monopoly. In justice to the States it is important to note that the principle of a secretariat has not been in great dispute. The value of such an organisation could hardly be questioned. What has probably deterred the States more than any single factor is the concern that the Secretariat might become an informal adjunct of the Commonwealth Treasury. This certainly was their dominant thought during the pre-war discussions.[38]

[37] For the circumstances of his appointment see *Premiers' Conference* (October 1938); *Premiers' Conference* (March 1939); (1939) 162 Commonwealth Parliamentary Debates, 2343; and E. R. Walker, The Australian Economy in War and Reconstruction (1947), 47, 95.

[38] See generally J. A. Maxwell, *The Recent History of the Australian Loan Council*, in (1940) 6 Canadian Journal of Economics and Political Science, 37; Professor D. B. Copland, in Sydney Morning Herald of 29th August

Until 1940, the chief function of the Loan Council was generally implicit in the purpose of its creation—namely, to control and co-ordinate the public borrowing of the Commonwealth and State governments. To this end it was mainly concerned with the *total* loan demands of the Commonwealth and State governments; the *maximum* amount which could be borrowed at reasonable rates and conditions; and the *allocation* of the agreed sum between the various governments. The Council was not directly concerned with the merits of any proposed loan expenditure. Its control of public investment was purely quantitative. Within the limits of its grant each State was free to pursue an independent spending policy.[39]

Today it remains substantially correct to say that the Loan Council's function is primarily to control the volume, not the quality, of public investment. But with the creation and continuance of the Co-ordinator-General's office, a subtle change has taken place in the Council's original conception. Evaluation of this change is difficult. From all accounts it appears that *some* degree of qualitative control (or what is in effect the co-ordination of spending) has now become an element of the Loan Council's activity. But to *what* degree it is hard to determine from the available material. Certainly, during the war, the Council, through the Co-ordinator-General, exercised a fairly rigorous control over public investment.[40] Since 1946, however, there has been little sign of anything like the same degree of scrutiny or regulation. The rationale of the Co-ordinator-General's original appointment has changed; and the continuation of his office is probably due, first to the success of the war-time practice, and secondly to the implicit understanding that his role is essentially advisory. Officials have been at great pains to emphasise that anything more, any pretence by the Council to exercise real control would wreck even the mild scrutiny given at present to the Commonwealth and State works programmes. The Co-ordinator-General's role, therefore, must not be exaggerated. Clearly he must tread with great caution.

1938; Australian News Digest of 8th September 1938. See also Forgan Smith (Queensland) at Premiers' Conference (1938), 9:— "Why should we not have a secretariat not responsible to any one government which would make investigations regularly and be in a position to make recommendations to the Loan Council as a whole in regard to the mobilisation and control of credit available to industry and for the development and defence of the country?"

39 One qualification may consist in the indirect control exercised by the Commonwealth over the "mendicant" states—Tasmania, South Australia, and Western Australia.

40 See Walker, *loc cit.*

The sensitivity of State Premiers to direction is notorious. They are more inclined—as one official put it—"to tell 'X' what they propose to do than wait for his advice." If the Co-ordinator-General ever succeeds in deflecting or postponing a particular project it is entirely by persuasion, no more. For one thing is eminently clear—that if fiscal centralisation in Australia is well advanced it is still far from the point where the Commonwealth or any other body can direct the specific use to which a State should apply its loan funds.

The jurisdiction of the Loan Council may be briefly stated. Strictly, according to the terms of the Financial Agreement, its jurisdiction does not embrace *all* classes of public borrowing.. The exceptions in order of importance are (a) Commonwealth loans for defence purposes; (b) borrowing by local and semi-governmental authorities; and (c) borrowing for "temporary" purposes. In practice, however, the first two classes of loans have been brought within the purview of the Council. The omission of local and semi-governmental borrowing proved a serious defect. It gave the States an opportunity to circumvent the Council's control by placing a number of important State activities—for example, water, sewerage, and tramway boards—outside the budget. And this, together with the enormous growth of borrowing by these bodies immediately prior to the war, rendered any comprehensive control and co-ordination extremely difficult. To meet this situation, therefore, a "gentlemen's agreement" was concluded in 1939 to bring all estimated borrowing by semi-governmental bodies (whether for new money or for conversion purposes) into account.[41] The exclusion of Commonwealth defence loans was more justifiable. By their very nature they enjoy a special priority over

[41] The terms of the "informal" agreement, made in July 1939, are as follows:— "Each Government represented on the Loan Council agrees:

1. That in future all loan moneys which are required by (a) that Government or (b) any municipal, local or other public authority of the Commonwealth or State, as the case may be (in this resolution referred to as a semi-governmental authority), shall be obtained only from moneys raised in accordance with clauses 4, 5 or 6 of part I of the Financial Agreement, or from moneys raised by a semi-governmental authority with the consent of the Loan Council.
2. That it will not, without the prior approval of the Loan Council, guarantee any loan raised or to be raised by any semi-governmental authority (not being a guarantee of an overdraft to a body established under the law of a State for the organised marketing of produce).
3. That it will from time to time furnish to the Secretary of the Loan Council particulars of all guarantees given by it to bodies other than semi-governmental authorities.
4. That nothing in the foregoing provisions of this resolution shall prevent (a) any semi-governmental authority from raising in any financial

every other class of borrowing. From the States' viewpoint, however, this exclusion could prejudice their interests. In the existing connotation of "defence", for example, it empowers the Commonwealth to borrow for almost any purpose without Loan Council scrutiny; and in this way the Commonwealth could easily manoeuvre its demands to "dampen" State loan programmes. For this reason it appears that a second "gentlemen's agreement" was concluded in August 1951 whereby the Commonwealth undertook to submit its total loan requirements to the Council. In regard to the third class of borrowing, the position is somewhat obscure. The specific character of borrowing "solely for temporary purposes" is not defined in the Financial Agreement. Originally it was probably intended to free every form of short-term accommodation from the Council's control. And even now this power is sufficiently alive in law to invalidate any Commonwealth legislation which might impair this governmental right to short-term credit. In practice, however, since bank overdrafts to bridge revenue deficits were brought within the control of the Loan Council during the '30's, the residuary privileges of the States in regard to "temporary borrowing" are now virtually negligible.[42]

To this brief review of the apparatus and scope of the Loan Council, one final note. The executive agency of the Council for the purpose of borrowing is the Commonwealth. Once the Loan Council has decided on a particular course of action, loan operations are conducted solely by the Commonwealth. The securities issued are Commonwealth securities, signed by the Commonwealth Treasurer as Chairman of the Loan Council, and are redeemable at the Commonwealth Bank. The principal operative exceptions to this rule are, first, the right of a State—subject to the Council's decision regarding the rate of interest and other charges—to borrow from any "authorities, bodies, funds or institutions" within its territory, and from the "public by counter sales of securities." In this class of local borrowing,

> year for its own purposes (other than for the purpose of repayment to a Government) a sum or sums totalling less than £100,000, provided that where the amount exceeds £50,000 particulars thereof are communicated to the Secretary of the Loan Council immediately upon approval of the loan being given; or (b) the Commonwealth or a State from guaranteeing the indebtedness of any semi-governmental authority to an amount or amounts not exceeding in the aggregate £100,000 in any one financial year."

42 See *The Case of the People of Western Australia*, (1934, Government Printer of Western Australia), 84-86; N. Cowper, *op. cit.*, 125-126; Mitchell, *op. cit.*, 56-61, and Supplement, vi; and *Melbourne Corporation v. The Commonwealth*, (1947) 74 C.L.R. 31, at 63-66.

however, the Commonwealth remains the guarantor, and Commonwealth securities are issued on all moneys raised independently by the State. Secondly, local and semi-governmental authorities—though subject to the Loan Council's scrutiny—make their own loan arrangements, and borrow on their own security.

IV. The operation of the Loan Council.

To speak of the Loan Council's procedure at once creates a vision of some regular and ordered mode of conducting the business of public borrowing. If there is a detailed pattern in this sense, the Financial Agreement itself gives only the slenderest indication of it. The Agreement simply requires that the "Commonwealth and each State will, from time to time, submit to the Loan Council a programme setting forth the amount it desires to raise by loans during each financial year." It specifies the broad nature of the statement; and it vests the Loan Council with the complete discretion—except in such matters as voting—to frame its own rules for the conduct of business at its meetings. Whether the Council has formulated a set of rules in these matters or whether there is simply a conventional pattern of procedure is not easy to determine. The exact proceedings of the Loan Council, no less than the activity of the Cabinet, are particularly an enigma. Its meetings are shrouded with considerable secrecy. The Council generally meets in the House of Representatives in Canberra behind locked doors. Its minutes are confidential.[43] Beyond a brief press "hand-out", press "imagination", and the occasional "indiscretions" of some of its members, little is known of its actual proceedings. We have made an attempt to reconstruct some elements of its operations from a number of secondary sources[44] and chance conversations with public officials. What follows, however, pretends to be no more than a skeletal and diffident outline of the Council's activity.

The Loan Council usually meets on the average twice a year for periods varying from two to three days. Its longest meeting was in May 1952, when it sat for three days and the session lasted 35 hours. The principal meetings generally take place in Canberra before the

[43] See *Mitchell*, *op. cit.*, 55. In his view it was "almost essential that if the Loan Council did not sit in public, it must at least, after each sitting, publish minutes of what it has decided, so that intending lenders may see that the Commonwealth or State is borrowing within the amount fixed by the Loan Council, and in accordance with the maximum limits as to interest, etc. (if any), fixed by it."

[44] See Maxwell, *op. cit.*, and Giblin, *loc. cit.*

end of each financial year on a date mutually convenient to the Commonwealth and the States. But further meetings are frequently convened for purposes of supplementary borrowing or, for example, if the Council finds that owing to the conditions of the loan market it cannot raise the required sum in one transaction, it will generally agree to meet at a later stage to reconsider the position. On occasions, also, where policy has been settled at the principal meeting, the Commonwealth may secure State approval to specific operations by correspondence instead of convening a further meeting of the Council.

The formal information submitted to the Council before each meeting is partly defined by the Financial Agreement and partly by practice. Prior to 1940 each member sent the Secretary of the Council a statement of its loan requirements which mainly contained the information required by the Financial Agreement. These statements broadly listed the estimated loan expenditure under two principal headings:—public works, and budgetary deficits (if any). The specific nature of the public works was not disclosed, except under such general heads as railways, bridges, and so on. If some piece of detailed information was volunteered it emerged only indirectly in the course of discussion in the Council to reinforce the particular claims of a State; for example, "we are committed this year to the construction of "X" reservoir . . . " or "we cannot delay the construction of a railway from "A" to "B" any longer.[45]

Since 1940 three changes have been introduced, two of which have radically expanded the body of information available to the Council. In the first place the provision requiring each State to submit a statement of its loan requirements "for each financial year" has been slightly amended to bring the formal requirements of the Agreement into line with practice. The Commonwealth Prime Minister explained this purely technical amendment in these terms:—[46]

> The Financial Agreement prescribes that the Commonwealth and each State will from time to time submit to the Loan Council a programme setting forth the amount it desires to raise by loans for each year. It has not been practicable to

[45] See L. F. Giblin, *loc. cit.*, 39: "Each State indicates what its needs are. The Loan Council takes no cognizance of that. One State says it wants 3,000,000 pounds, and that is accepted; it is not examined in any way, nor is any question asked as to the way in which the money is to be spent . . . It simply says it wants £3,000,000."

[46] J. B. Chifley, in (1944) 180 Commonwealth Parliamentary Debates, 1897.

relate the borrowings during a year to the actual loan expenditure during that year. Public loan raisings must be arranged at convenient intervals, and it has been customary for moneys to be borrowed towards the end of each financial year sufficient to meet the requirements during the early part of the new financial year until a further loan raising becomes practicable. This procedure is not strictly in accordance with the Financial Agreement, and it is now proposed in the amending agreement that the loan programmes to be submitted by the various governments shall be the programmes of amounts desired to be raised during each year and not loans raised for each financial year. This involves no alteration of procedure, but merely brings the provisions of the agreement into line with the present practice."

In the second place we have already noted the important practice initiated early in the war of submitting detailed public works programmes to the Council through the office of the Co-ordinator-General. Thirdly we also noted the submission of details of local and semi-governmental borrowing to the Council. The present position, therefore, appears to be this:— each of the seven governments prepares three main statements—(a) a statement of estimated loan expenditure in accordance with the Financial Agreement as amended in 1944; (b) a statement of estimated loan expenditure of all semi-governmental and local authorities in accordance with the "gentlemen's agreement" of 1939; and (c) a detailed programme of public works corresponding to the total estimated loan expenditure of (a) and (b) in accordance with the practice initiated in 1941. The first two statements are sent directly to the secretary of the Loan Council, and the detailed works programme is sent to the Co-ordinator-General of Works for examination and report to the Council.[47]

[47] The programme of works is prepared in the following way: Each State department and each semi-governmental and local authority make a detailed statement of their proposed public works for the ensuing year on standard forms and submit this information to the State Co-ordinator of Works; at the same time a copy is sent to the Co-ordinator-General of Works in Canberra. The State Co-ordinator consolidates the individual requirements of the various administering authorities (semi-governmental and local authorities are collated separately) and submits the whole as the State programme of works to the Co-ordinator-General. The latter then, in turn, with the assistance of a small staff, supplemented by frequent consultations with the State Co-ordinators, and (if necessary) the State Premiers, examines and collates the States' programmes into a consolidated national programme of works for submission to the Council with his report and recommendations.

The uniqueness of the Loan Council, and the aura of secrecy which surrounds its meetings, tend to create an impression that its proceedings too may partake of the unusual. On closer examination of the available material, however, the anticipation of the unorthodox is dispelled. The opening stages of a Loan Council meeting conform to the normal "committee" procedure of almost any executive body. The Council is opened by reading the formal notice convening the meeting. The minutes are read and confirmed. The Secretary circulates a number of financial statements which set out the budgetary position of each government, the tentative figures of the Commonwealth and State loan programmes, the estimated funds available, the consolidated works programme of each State, the Co-ordinator-General's report, and any memoranda prepared by the Commonwealth and States.[48] The Chairman may give a brief report of any administrative action taken by him in relation to matters arising out of the Council's previous meeting. And then, following this routine preamble, the Council turns to its main business—the settlement of the Commonwealth and State loan programmes for the year.

In this task, again, the procedure of the Loan Council is distinguished by little from the general conference technique of any ministerial council. There is first, as in every case, a statement of Commonwealth policy, its appreciation of the loan market, the conditions of the national economy, and sometimes at this stage its judgment of the total loan demands; then following the Commonwealth each other member of the Council presents his State's case. This preliminary stage is, in effect, no more than the elaboration of seven individual "briefs" in which the fiscal position of each member, its revenue and loan finance, etc.—already outlined to the Council in the formal information submitted by each member—is now fully developed. It has been usual at this stage also for the Co-ordinator-General—who attends each meeting of the Council—to give a brief analysis of the total programme of works in relation to the availability of labour, material resources, and any other factors which may affect the estimated programme. Then, once the fiscal position of each government has been fully presented to the meeting, the Council moves to the determination of its two major problems—(a) the

[48] Note that, prior to 1944, the Council formally elected the Commonwealth Prime Minister to the chair; but since then an amendment of the Financial Agreement has given permanent status to the Prime Minister as Chairman of the Council. See (1944) 180 Commonwealth Parliamentary Debates, 1897, and 218 Victorian Parliamentary Debates, 2264.

amount to be raised, in what portions, and at what periods, and (b) the mode of distribution.

If the Loan Council's operation has tempted the view that this institution is something more than its title suggests—that it should be renamed the "Australian Finance Council"—it is due, almost entirely, to the range of the discussions which, each time, precede its first decision—whether the combined loan programmes can be met, and if not, then the maximum sum which can be raised at "reasonable rates and conditions."[49] It is clear that before it makes this decision, the problem of capital demand and capital supply is discussed against the whole background of the prevailing monetary and economic condition of the Commonwealth and each State. It was certainly not intended in 1927 that this body should evolve into a national finance council. Yet, in the very nature of the first decision it must make, it is difficult to see how the Council could hope to discharge its function without engaging—however briefly—in a general debate on these matters. It is here, moreover, at this inflammable stage of its proceedings (as much as, and frequently more than, in the apportionment of the agreed total loans) that a violent controversy may often ensue in which conflicting policies of public investment, fiscal management, personal enmities, party politics, and the inevitable relations of Commonwealth-State finance are thrown to the surface.

To decide the total loan programme, the Council is free to draw upon any information—beside Treasury opinion—and consult any institution.[50] During the "depression", for example, the Loan Council relied extensively on the advice of a number of prominent economists —notably Professors Giblin, Copland, and Melville. And even now, according to one source, "Professor 'X' is generally to be found on the fringe of the Council." The one institution, however, which (until at least 1940) exercised a formidable influence at this stage of the discussions was the Commonwealth Bank. Its highly controversial activity in the formulation of the Premiers' Plan is now a matter of history, and we do not propose to resurrect it. Some indication of its immediate pre-war role, however, is provided by Professor Giblin's evidence to the Rowell-Sirois Commission on the working of the Loan Council.[51] "Nominally", he said, "the Loan Council is

[49] See, for example, Forgan-Smith's suggestion that the Loan Council should be renamed the "Australian Finance Council", referred to by D. B. Copland and C. V. Janes in *Cross Currents in Australian Finance*, 15-16.
[50] Mitchell, *op. cit.*, 51.
[51] Giblin, *loc. cit.*, 39.

supposed to make up its own mind . . . and decide whether the total loan programmes can be raised or not. In practice, however, the Council does not like risking a loan unless it is underwritten", and the "only body in a position to underwrite it is the Commonwealth Bank." Hence, it was common for the Chairman or an *ad hoc* committee to enter into negotiations with the Bank. How far this practice may disclose the realities of pre-war borrowing in Australia is again illumined in the outburst of a State Premier:— "The Loan Council is purely a farce. This is what happens. State ministers are dragged from the corners of Australia with our officers. For two days we talk together and put our genuine requirements into shape. It is time and trouble wasted. At the end of all our moulding and adjusting the Commonwealth Treasurer (Mr. Casey) telephones the chairman of the Bank Board. Telephones, mind you!"[52] This incident may or may not be typical of pre-war Council meetings. To this picture, however, two brief notes must be added. In the first place, it is quite clear that constitutionally the approach to the Commonwealth Bank, as Giblin hastened to point out to the Rowell-Sirois Commission, was an "accidental side issue."[53] "The Loan Council has complete authority to determine the maximum which can be borrowed and proceed to raise it. Thus, for example, if the Commonwealth Bank had refused to underwrite the total sum required by the Council, the Council could have floated its own estimated total loan, and taken their chances on the market." Secondly, the present influence of the Commonwealth Bank on the Council is slight. It underwrites the Council's operations and remains its most influential source of advice on the state of the loan market. But since the reconstitution of its governing board and the centralisation of credit policy in 1945, it has lost, for the time at least, the power to command the Council's investment policy.

Once the total sum to be raised is settled, the Council turns to its allocation among the members—a stage stigmatised by one irreverent official as the dog-fight. Clearly, the problem of allocation does not arise where the total loan requirements of the Commonwealth and the States can be satisfied. But where the Council decides that the total cannot be raised on reasonable terms—and this has been almost invariably the case—the meeting then determines the sum which can be raised, and proceeds to scale down the original loan demands. Here, the provisions of the Financial Agreement are

52 Quoted by Maxwell, *op. cit.*, 28.
53 Giblin, *loc. cit.*, 39.

simple enough. If there is *unanimity,* the Council is free to make whatever allocation it desires. In the absence of unanimity, however, the allocation is automatically determined in accordance with a statutory formula.[54] The economic critiques of the formula need not concern us.[55] The formula has never been applied.[56] Invariably, after intensive "horse-trading", agreement has been reached. On one occasion at least (1935) it appears that the Council, prior to discussing the apportionment of loan funds, instructed the Under-Treasurers to examine and report on the application of the formula to the agreed total. In this instance their report showed the results of applying the formula and alternative methods of distribution. The instructions to the Under-Treasurers in this case, however, must not be confused with a final application of the formula to settle an irreconcilable situation. On this occasion it probably served to define the area of dispute more closely, and thereby tied the negotiations to a concrete basis. In general practice, the weakness of the formula—despite some recent amendments—is recognised. The needs of the Loan Council are variable, and the formula is rigid and artificial. Yet it cannot be dismissed altogether. Paradoxically, from its very weakness springs its main strength, for in the threat of its application lies a constant inducement to compromise.[57]

With the resolution of these two problems—the amount to be raised, and its allocation—the business of the Loan Council is virtually at an end. The Commonwealth is then formally authorised to raise the necessary funds and settle the details of underwriting with the Commonwealth Bank. All that remains is to consider the requirements

54 Broadly, the apportionment is made as follows: First, the Commonwealth is entitled to one-fifth of the agreed total; secondly, each State is entitled to the same proportion of the total sum available to the States (after meeting the Commonwealth needs) as "the net loan expenditure of that State in the preceding five years bears to the net loan expenditure of all the States during the same period." In either case, however, the Commonwealth or any State may accept less than its allotted share. Furthermore, in the event of the formula being applied, the term "net loan expenditure" does not include expenditure for the funding of revenue deficits, or to meet revenue deficits, or "any specified class of expenditure which the Loan Council by unanimous decision declares shall not be included . . . "

55 Maxwell, *op. cit.,* 26-28.

56 See J. B. Chifley, (1944) 180 Commonwealth Parliamentary Debates, 1898.

57 See Giblin, *loc. cit.,* 44-45:— "Always in fact some compromise has been reached, but it is only because there is the automatic agreement behind it . . . Generally, there is a good deal of give and take and adjustments . . . have fairly solved the problem."

of the various local and semi-governmental authorities (normally a brief matter) and other business which may require the Council's attention—for example, to arrange for any "conversions, renewals, or redemptions" of existing loans, to approve the conditions of any local borrowing by a State, and so on.

To complete this short sketch of the Council's operation one other factor must be noted, namely, the nature and significance of the Council's voting arrangements. In essence the Financial Agreement provides that in *all* matters, except (a) the apportionment of loan funds, and (b) consent to independent borrowing by a State outside Australia, disputes are to be resolved by a *majority* vote; for this purpose the Commonwealth has two votes and a casting vote by virtue of its special position under the Agreement, while each State is given one vote only.[58] Thus, for example, in such matters as the total sum of money to be raised, the rate of interest, the conditions of the loan, the source of borrowing, questions of procedure, the nature of the information to be submitted to the Council, and so on, decisions may be made by a simple majority. In the case of the two principal exceptions (a) and (b), however, *unanimity* is essential.

This arrangement has generally raised two main questions; the extent to which voting is used in the Council, and the extent to which voting—if and when used—corresponds to party affiliations. A precise answer, of course, could only be given if the Council's minutes were thrown open to examination. But, short of this, some rough approximation to the position may be made through a number of scattered references. In the first place, it is quite clear that voting has taken place, and that it has only been used—notably in May 1952—for matters of major policy.[59] On the question of frequency however, Professor Giblin's evidence to the Rowell-Sirois Commission in 1939,[60] Professor Maxwell's paper, *The Recent History of the Australian Loan Council,*[61] and the opinions of a random number of senior officials clearly suggest that the dominant tendency in the Loan Council is to resolve conflicts by compromise rather than voting. On occasions there has been an unofficial counting of heads; but for the most part, there is a general desire to avoid pushing any important question through on the basis of majority voting.

58 Financial Agreement, clauses 3 (m) and 4 (b).

59 See an oblique reference, for example, in (1944) 114 Western Australia Parliamentary Debates, 2144; and note E. R. Walker, *op. cit.*, 95.

60 See Giblin, *loc. cit.*

61 Maxwell, *op. cit.*

The Council prefers to talk around a subject until agreement is reached. If voting is applied or threatened in the case of some fundamental divergence, however, does the Council divide on party lines? The bulk of opinion we sought is agreed that voting alignments are rarely, if ever, related to the political complexion of the Council. This view is generally consistent with the character of the States' behaviour in the consultative councils, and certainly it is exemplified in the whole conflict over Federal-State financial relations. Indeed, it is too simple to presume that the individual self-interest of each State is so tenuous that party allegiance alone is sufficient to dictate its alignment in the Council. If voting in the Council does not correspond to party affiliation, are there any significant alignments on the Council at all? Are the only alignments, as one cynic remarked, "along parallels of latitude?" Whatever the occasional groupings of States, one clear division in the Council is persistent—notably the cleavage between the Commonwealth and the States. The whole tenor of pre-war Council discussions accentuated this division, and the post-war meetings have contributed further evidence of it. True, it may vary in its intensity from one period to another, but its presence is unmistakable.[62] We need scarcely elaborate the reasons, for the drama of Federal-State financial relations is continually re-enacted on the stage and in the wings of the Loan Council. There the Commonwealth enjoys a position of strength under the Agreement, and to this it adds the full bargaining force it derives from its present control of central bank credit policy, its aggrandisement of income taxation, and its partial influence over the three "mendicant" States. With few exceptions this power has normally enabled the Commonwealth to "bring about a compromise solution" of most disputes which have arisen in the Council.

V. The enforcement of Loan Council decisions.[63]

The pre-eminent constitutional feature of the Australian Loan Council is the *final and binding* effect of its decisions. The question

62 See, for example, the remark of the then Premier of New South Wales, Mr. J. McGirr, at the August 1951 meeting of the Loan Council (as reported in Sydney Morning Herald of 18th August 1951, on page 4):—"The Commonwealth side-stepped every State request put to it. On some occasions the Commonwealth's secretive attitude made discussion pointless and time-wasting. I refer particularly to our two days of Loan Council discussion. The Commonwealth refused repeatedly to reveal what cut it wanted until the last minute. Discussion became farcical under those circumstances . . . "

63 The legal implications of the Financial Agreement are fully examined by Sir Edward Mitchell in *What Every Australian Ought to Know* (1931)

we wish to examine here very briefly is—what are the nature and ambit of its executive power? We noted earlier that the Council's authority rests on the provisions of sec. 105A of the Constitution and the Financial Agreement. The relevant provisions which bear directly on this issue are as follows:—

First, sec. 105A provides that,

> (1) The Commonwealth may make agreements with the States with respect to the public debts of the States, including—
>
> (e) the indemnification of the Commonwealth by the States in respect of debts taken over by the Commonwealth: and
>
> (f) the borrowing of money by the States or by the Commonwealth, or by the Commonwealth for the States.
>
> *(3) The Parliament may make laws for the carrying out by the parties thereto of any such agreement.*[64]
>
> (5) Every such agreement and any such variation thereof shal be binding upon the Commonwealth and the States parties thereto notwithstanding anything contained in this Constitution or the Constitution of the several States or in any law of the Parliament of the Commonwealth or of any State.

and its *Supplement* published in 1933 following the *Garnishee Case* (the *Supplement* embodies Sir Leo Cussen's views on Mitchell's book.) This publication, written to reassure the investors of the complete constitutional security offered by the Financial Agreement, in the midst of Lang's threats of default on overseas interest payments, is an exceptionally interesting legal and political document. The author's interpretation of sec. 105A of the Constitution was confirmed by the majority opinion in the *Garnishee Case;* and, more recently, echoes of Mitchell's opinion of the consequences of the Financial Agreement on banking legislation (see c. X, 64-67) were heard in the *Melbourne Corporation Case,* (1947) 74 C.L.R. 31, and the *Bank Nationalisation Case,* (1948) 76 C.L.R. 1. The author was intimately involved in the events of this period. His account of his activities in the preparation of the Debt Conversion Agreement of 1931, for example (published by him as a confidential memorandum), throws some rather interesting light on the manoeuvres of the time. The author appeared as counsel for the Commonwealth in the *Garnishee Case;* and there is little doubt that he was closely consulted beforehand by the Commonwealth Attorney-General and Solicitor-General in planning the Financial Agreements Enforcement Act.

64 Italics added.

The Financial agreement provides:—

Part I, clause 3 (n). A decision of the Loan Council in respect of a matter which the Loan Council is by this Agreement empowered to decide shall be final and binding on all parties to this Agreement.

clause 4 (a). Except in cases where the Loan Council has decided under sub-clause (b) of this clause that moneys shall be borrowed by a State, *the Commonwealth,* while . . . this Agreement is in force *shall, subject to the decisions of the Loan Council . . . arrange for all borrowings for or on behalf of the Commonwealth or any State,*[65] and for all conversions, renewals, redemptions, and consolidations of the Public Debts of the Commonwealth and of the States.

clause 4 (d). While . . . this Agreement is in force, moneys *shall not*[65] be borrowed by the Commonwealth or any State otherwise than in accordance with this Agreement.

Part IV, clause 3. Each State agrees with the Commonwealth that it will by the faithful performance of its obligations under this Agreement indemnify the Commonwealth against all liabilities whatsoever in respect of the public debt of that State taken over by the Commonwealth . . . and in respect of all loans of that State in respect of which this Agreement provides that sinking fund contributions shall be made.

In regard to the conduct of loan operations we noted that the Commonwealth is the executive agency of the Loan Council. What is the Council's executive agency, however, for the enforcement of the rights and duties created by the Financial Agreement? For example, if a State attempts to borrow independently in defiance of the Council, or if with the Council's consent to borrow independently it offers a higher interest rate than sanctioned by the Council, or if the Commonwealth refuses to arrange loans for the amount agreed

[65] Italics added.

by the Council, or if it proceeds to borrow in contravention of the conditions laid down by the Council, who is to enforce these rights and duties, at whose direction, and by what remedies?[66]

The Financial Agreement makes no provision for its enforcement. Let us therefore approach our problem by considering two situations; (a) the enforceability of the Agreement in the two years (1927-1929) prior to the insertion of sec. 105A in the Constitution; and (b) the nature of the changes effected by sec. 105A. In the first place, it is clear that whatever the doctrine of the indivisibility of the Crown predicates in common law, or whatever the immunities of the Crown in Australia from suit prior to 1901, the implications of a federal union required at least one major exception—the actionability of the mutual rights and obligations between the Commonwealth and the States.[67] To this end, sec. 75 of the Constitution invested the High Court with jurisdiction *in all matters* in which the Commonwealth or a person suing or being sued on behalf of the Commonwealth is a party, between States, or between States and a resident of another State. Sec. 78 of the Constitution empowered the Commonwealth Parliament to "make laws conferring rights to proceed against the Commonwealth or a State in respect of matters within the limits of the judicial power"; in pursuance of this power, Part IX of the Judiciary Act 1903-48 amplified the powers of the High Court and the rights of parties in "suits by and against the Commonwealth and the States." The precise foundation of the High Court's jurisdiction in actions between the Commonwealth and the States may have been subject to some minor differences of opinion; what has rarely been in judicial dispute is the *range* of its jurisdiction. "The words 'in all matters' are the widest that can be used to signify the subject matter of the Court's jurisdiction . . . "[68] Again, "a matter . . . in order to be justiciable, must be such that a controversy of like nature could arise between individual persons, and must be

66 We are not concerned here with the enforcement of the Agreement by any other parties than the signatories. For the possible rights of public creditors under the Agreement, see Mitchell, *op. cit.*, 31, and *Supplement*, 12-13.

67 See *South Australia v. Victoria*, (1911) 12 C.L.R. 667, per Higgins J. at 744:— "It is true that, within its own limits, a State represents the Crown as against private persons; but it cannot represent the Crown in contests between itself and other States which equally represent the Crown." See also *Commonwealth v. New South Wales*, (1923) 32 C.L.R. 200, per Isaacs, Rich, and Starke JJ. at 207-216, and their incisive remarks regarding the so-called "sovereign" character of the States at 208-210.

68 *Ibid.*, per Isaacs, Rich, and Starke JJ. at 212.

such that it can be determined upon principles of law. *This . . . includes all controversies relating to the ownership of property or arising out of contracts."*[69]

From this, it needs little to infer (i) that the contractual rights and duties of the Commonwealth and the States under the provisional Financial Agreement of 1927 prior to the insertion of sec. 105A in the Constitution (a) were fully actionable in the High Court, (b) *by any of the parties to the Agreement,* and (c) the Court was entitled to give judgment and grant relief appropriate to the cause of action; and (ii) that insofar as the Loan Council could be said to have a coercive power it rested not in the Council *per se*, but in the right of each member to enforce the Council's decisions at its own discretion. Thus, for example, if a State attempted to borrow money independently, and in further contravention of the Agreement proceeded "to invite loan subscriptions by the issue of a public prospectus" (presuming, of course, that some institution or person was prepared to incur the possible risks of subscribing to an *ultra vires* loan), the Commonwealth, or for that matter any other State, could probably obtain an injunction against the offending State and its officers. Conversely, if the Commonwealth refused to convene a meeting of the Council when requested by three or more States, or if it refused to borrow the sum of money agreed to by the Loan Council, there is probably little doubt also that the State could enforce its obligations under the Agreement through the normal judicial remedies available in the High Court.[70]

To these mutual rights of enforcement through the Courts, one

[69] *South Australia v. Victoria,* (1911) 12 C.L.R. 667, per Griffith C.J. at 675 (italics added).

[70] The question of a Commonwealth refusal to borrow a sum of money it believed in excess of the market capacity indirectly arose at the May 1952 meeting of the Loan Council. The Commonwealth was outvoted by the States, and it was suggested that the Commonwealth was bound to borrow the sum irrespective of its opposition. In 1932, Mitchell had expressed the view (*op. cit.*, 20, 52, 54) that Clause 4 (a) of Part I was binding on and enforceable against the Commonwealth. "That clause vests the Commonwealth not merely with the power, but with the duty of arranging for all borrowing . . . " except in cases excluded by the Financial Agreement. And further, " . . . as the power to borrow given to the Commonwealth under Clause 4 (a) is expressly made subject to the decision of the Loan Council, that gives an extra ground for holding compliance with any such decision a condition precedent." The practicability of enforcing this obligation where the Commonwealth is responsible for raising loans is of course highly dubious. This aside, however, the States could probably seek a declaration of its liability under Clause 4 (a); and certainly the High Court has the power to issue a mandatory injunction against the Commonwealth.

crucial limitation must be noted, namely, the prohibition of sec. 65 of the Judiciary Act that *no execution or attachment, or process in the nature thereof shall be issued against the property or revenues of the Commonwealth or a State . . .*[71] The nature of this prohibition is clear enough; it simply affirms the vital constitutional doctrine that the liabilities of the Crown (whether in right of the Commonwealth or a State) are subject to the implied condition that the funds necessary to discharge these liabilities must be appropriated by Parliament.[72] Thus, for example, in the event of default by a State in its interest payments under the Agreement, the Commonwealth could sue the State; but its power to exact payment under a judgment in its favour would depend on the action of the State Parliament. Normally, of course, this privilege of the Crown is scarcely a "question of any importance, for usually provision is 'readily and promptly' made to satisfy such an obligation."[73] In the rare contingency of a State's refusal to comply with the judgment, however, no power of the federal legislature or judicature could levy execution. The sole remedies then lay in the realm of politics, not of law.

If this view of the position prior to the amendment of the Constitution is correct, how did sec. 105A affect it? The enforceability of the Financial Agreement has been tested in one instance only—the celebrated *Garnishee Case* in which the State of New South Wales unsuccessfully challenged the right of the Commonwealth Parliament to sequestrate its revenues in satisfaction of interest payments on which the State had defaulted. We need not recapitulate the familiar story of Mr. Lang's defection. It is an episode of countless facets. For us, the chief interest of this case rests in its examination of the nature and scope of sec. 105A of the Constitution, the power from which the Commonwealth Parliament purported to exercise the right to take from the taxpayers of New South Wales "moneys payable by them to the State in satisfaction of the payment which the State had failed to make" under the Financial Agreement.

The instrumental federal statute—the Financial Agreements Enforcement Act 1932[74]—set up detailed machinery of execution against a defaulting State and prescribed two methods of setting it in motion;

71 Italics added.

72 See *New South Wales v. Commonwealth, No. 1* (the *Garnishee Case*), (1932) 46 C.L.R. 155, per Rich and Dixon JJ. at 176, 177, and Starke J. at 185.

73 *Ibid.*, per Starke J. at 185.

74 But for the real doubt that anything less than direct execution would remedy Lang's default, the Commonwealth would have probably taken the normal judicial procedure to recoup itself.

first, by a summary process whereby on the publication of the Auditor-General's certificate that a debt was due to the Commonwealth under the Financial Agreement, the Attorney-General could apply to the High Court for a declaration of the debt; and thereupon the declaration was to operate both as a judgment of the Court and as a charge on the revenues of the State; and secondly, by a joint resolution of the two Houses of Parliament where, in their opinion, urgency required immediate execution. The unique and startling character of these measures is manifest. The Act was impugned on three main grounds: (a) sec. 105A did not confer a power of enforcement on the Commonwealth Parliament; (b) if it conferred a power of enforcement it was conditioned by the principle that the liabilities of the Crown are subject to parliamentary appropriation; and similarly (c) if sec. 105A conferred a power of enforcement it could not be exercised discriminately in favour of the Commonwealth against the States.

A majority of the Court, Rich, Starke, Dixon, and McTiernan JJ. (Gavan Duffy C.J. and Evatt J. dissenting), rejected these arguments. In the joint opinion of Rich and Dixon JJ., the validity of a Commonwealth law to sequestrate State revenues in satisfaction of its liabilities under the Agreement could be founded equally on sec. 51 (xxxix) in combination with sec. 105A (5), and on sec. 105A (3). In their view, sec. 105A (5) was crucial to the understanding of the Commonwealth power to enforce the Agreement. Its effect was "to make any agreement of the required description obligatory upon the Commonwealth and the States, to place its operation and efficacy beyond the control of any law of any of the seven Parliaments, and to prevent any constitutional principle or provision operating to defeat or diminish or condition the obligatory force of the Agreement."[75] And therefore once given that the contractual obligations under the Agreement were "absolute and independent of Parliamentary appropriation", then "the power conferred upon the Parliament by sec. 51 (xxxix) to make laws with respect to matters incidental to the execution of any power vested by the Constitution in the Federal Judicature clearly authorises laws for carrying into execution all the judgments which the judicial power has power to pronounce.[76] The legislation, however, could be validated also by sec. 105A (3) of the Constitution. This placitum was not simply designed to facilitate the performance of the Agreement, nor "to enable the Federal Parliament to establish later agreements as valid

[75] *Commonwealth v. New South Wales, No. 1,* (1932) 46 C.L.R. 155, at 177.
[76] *Ibid.,* 176.

and binding . . . "[77] It could effect both these ends; but its principal force was to authorise "the enactment of laws calculated to bring about the performance of the obligations created by the Agreement."[78] The opinion of McTiernan J. rested on a substantially similar view of the combined effects of sec. 105A (5), sec. 51 (xxxix), and sec. 105A (3). For him, "the imperious character of the language employed in" sec. 105A (5) renders certain the paramount force of any Financial Agreement to which the sub-section applies. "It restrains the Commonwealth and every State, which is a party to such an Agreement, from contravening the Agreement and raises the obligations, which the Agreement fastens on the parties, to the level of an obligation arising out of the Constitution itself. Those provisions in the Constitution of a State or in any law of the Parliament of a State, which require that Parliament must appropriate revenue before it can be lawfully applied in satisfaction of the obligation of of the State under any agreement or judgment, are clearly among the "things" which are overridden by sec. 105A (5)."[79] And in regard to sec. 105A (3), he said, "The true content of the power conferred by sec. 105A (3) was much debated at the hearing. I think that it extends to the enactment of laws which invoke the judicial power and aid it when it is exercised for the carrying out by the parties, or any one or more of them, of any relevant Financial Agreement. It may be that it is not every law which Parliament thinks expedient for coercing the parties into carrying out the Agreement that falls within the power conferred by sub-sec. 3. But the power at least extends to the enactment of such a law which is an aid to the execution of the judgment of the Court pronounced in legal proceedings arising out of the Agreement."[80] The opinion of Starke J. rested solely on the special executive force of sec. 105A (3).

We do not intend to discuss the correctness of the majority opinion; for this reason we have not adverted to the interesting dissentient judgment of Evatt J.[81] The *Garnishee Case* has clearly established that sec. 105A has altered the original position of the Commonwealth and the States in regard to the enforcement of the Financial Agreement in at least three material respects; first, sec. 105A has vested the Commonwealth with legislative power to create new and drastic extra-judicial remedies in aid of the ordinary judicial

77 *Ibid.*, 178.
78 *Ibid.*
79 *Ibid.*, at 228.
80 *Ibid.*, at 230-231.
81 *Ibid.*, at 192-227.

powers of enforcement—that is, the Commonwealth's power of enforcement is no longer limited to proceedings in the Courts and to attempted execution of any judgments given in its favour; secondly, the Commonwealth is not compelled to concede similar rights of extra-judicial enforcement to the States—that is, the power may be exercised discriminately; thirdly, the presumptions of secs. 65 and 66 of the Judiciary Act no longer operate in favour of a State in default to the Commonwealth under the Financial Agreement.[82] It it quite clear, therefore, that in the event of any breach of the Financial Agreement in regard to borrowing for which the normal judicial remedies are ineffective, the Commonwealth could marshal the full force of its legislative powers under sec. 105A to discipline a recalcitrant State.

What is not quite clear, however, is the effect of this decision on the States' rights of enforcement. Given that the States do not share the Commonwealth power to enforce the Agreement by extraordinary means, are the normal judicial remedies still available to them? The doubt is chiefly created by an obiter dictum of Starke J. In answer to the objection that the Financial Agreements Enforcement Act was a discriminatory exercise of sec. 105A (3), he remarked, "Further, it was said to be unlikely that a power of enforcement was given to the Commonwealth and none to the States. *The parties did not contemplate default but if default took place the Commonwealth seems the natural custodian of the power to enforce the Agreement and to provide remedies for non-performance, whether on its own part or on the part of the States. It cannot affect the construction of the clause that the States cannot dictate to the Commonwealth what remedies it should grant in case it makes default in performance of the Agreement.*"[83]

On the face of this dictum, a suggestion may be raised that the Commonwealth is not merely the *natural,* but the *sole* custodian of the power to enforce the Financial Agreement; and as a corollary, that the States are *wholly* dependent on the Commonwealth for remedies even in the event of default by the Commonwealth itself. If the dictum of Starke J. is at all susceptible to this construction then it seems to produce a somewhat curious situation. Let us note some of its possibilities: In the first place, the Commonwealth Parliament enjoys a complete discretion in the exercise of its special powers of enforcement under sec. 105A and sec. 51 (xxxix) of the Constitution.

[82] *Ibid.*, per Starke J. at 186-189, and McTiernan J. at 231.
[83] *Ibid.*, at 187 (italics added).

Whatever the particular breach of the Agreement there is nothing in the Constitution, or for that matter in the Agreement itself, to suggest that the Commonwealth should act on the instructions of the Loan Council, or that it should even seek its opinion. Thus, for example, if a State should attempt to float a loan in contravention of the Agreement, then whatever the reaction of the other States—or in effect the Council—the Commonwealth is free to accept, reject, or modify their views of the matter and to proceed to determine quite independently the appropriate course of action against the offender. This, of course, was originally the inherent right of every member of the Council prior to the amendment of the Constitution. But, whereas, prior to sec. 105A, the decisions of the Loan Council were enforceable by *any* of its seven members, now, in the event of a Commonwealth refusal to provide remedies for a breach whether on its own part or on the part of a State, the other members of the Council are left with no other remedies than political coercion.

Does the *Garnishee Case* support this view? Is the coercive power of the Loan Council vested exclusively in the Commonwealth? Is the Commonwealth now so privileged by sec. 105A that in the enforcement of the Financial Agreement it is both prosecutor and executioner? In our view, it is possible to sustain the majority decision without incurring the apparent consequences of the dictum of Starke J.—except for two cases we will note shortly. The *Garnishee Case,* we noted, determined that sec. 105A in combination with sec. 51 (xxxix) of the Constitution empowered the Commonwealth to enforce the Agreement by creating *new* or *additional* remedies in aid of the normal judicial process.

To say, however, that the Commonwealth is so advantaged *vis-a-vis* the States is fundamentally different from the view that the power of enforcement resides *solely* in the Commonwealth. Indeed, apart from this dictum, the majority judgments leave no sort of doubt that the rights of the States to enforce the Agreement against the Commonwealth (or for that matter the right of a State against any other State) through the Courts remain unaffected. McTiernan J. clearly inferred this.[84] Referring to the Financial Agreements Enforcement Act, he said, "These provisions do not assume to extinguish any liabilities to which the Commonwealth is subject under the Financial Agreements, nor do they deny any State the right to sue the Commonwealth and proceed to judgment and execution

[84] *Garnishee Case,* at 234.

according to law if it has a claim founded on all or any of the Agreements. The remedy given to the Commonwealth may appear to be more drastic and efficacious . . . but that circumstance is not, in my opinion, fatal to the validity" of the Act. In other words, in the event of a Commonwealth breach of the Agreement, the Loan Council is *not* dependent on the Commonwealth to provide remedies for "non-performance." Any one or all of its member States are quite free to seek redress through the Courts in the normal expectation that a judgment in their favour will be readily and promptly satisfied by the Commonwealth. Similarly, even if there were an informal understanding in the Loan Council that, in the event of a breach of the Agreement by any member other than the Commonwealth, the Commonwealth should take proceedings against the offender, then in the case of a Commonwealth refusal to act, the States could do so independently.

The one sense in which the presumed implications of this dictum could hold is in that class of abnormal cases where the normal judicial remedies might prove less efficacious—for example where there is a threat that (a) the Commonwealth or (b) a State against whom the Commonwealth refused to take any action may attempt to evade judgment. In these entirely exceptional circumstances, the States are clearly *dependent* on the Commonwealth Parliament to provide extraordinary remedies. But if these situations are technically possible, then it is equally clear that the notion of dependence in case (a) rests on an absurdity, and in case (b) on an improbability. In the first case there is an assumption that if the Commonwealth refused to observe the normal consequences of the judicial process, the Commonwealth Parliament would enact special legislation to compel its executive to do so—a position which the practice of parliamentary government could scarcely support; and in the second, there is the presumption that the Commonwealth in the case of a serious threat to the Agreement by a State would refuse to act.[85]

85 *Quaere* could the Commonwealth Parliament set up a system of enforcement which completely excluded the Courts? Or could the Commonwealth set up a system of enforcement which precluded the States from enforcing the Agreement through the Courts? In the *Garnishee Case*, counsel for New South Wales contended that the Financial Agreements Enforcement Act vested the Commonwealth with the power to circumvent the Courts, and the majority rejected this interpretation (see Rich and Dixon JJ. at 180; Starke J. at 190). If, however, the legislation had had this effect, or if the Commonwealth had attempted to deny to the States the use of the Courts, it is almost certain that the High Court would have nullified it.

VI. Some implications of the Loan Council—real and apparent.

One last inquiry now remains. The Australian constitution is founded on the dual principles of responsible government and federalism. How far is the Loan Council compatible with these principles? The question is of fundamental importance for here, without doubt, lies the root of much of the uncertainty surrounding this institution. Let us briefly examine this problem.

In his examination of the Financial Agreement Sir Edward Mitchell wrote:— "I infer from the whole of the provisions of Clause 3 *as well as* from the other provisions of Part I relating to the Australian Loan Council, that such Council and its members should act in a fiduciary capacity towards the whole of the Australian public, that is, *they are a body of public trustees to act in accordance with the well-established principles relating to public trustees, except insofar as such principles are modified by the express provisions of the First Agreement. That would include, in my opinion, that the representative of the Commonwealth and the representative of each State cannot—while acting as members of the Loan Council with discretionary powers of determining the different matters committed to them to decide—be lawfully fettered beforehand by specific instructions from the Prime Minister or Premier supporting them—how they were to decide.*[86] If this view depended exclusively on Sir Edward's interpretation of Clause 3 of the original Financial Agreement, it would be less than just to credit him with this opinion, and certainly pointless to examine it, now that the 1934 amendment of the Agreement has vested the Prime Minister and Premiers with sole membership of the Council unless they choose to exercise their power of appointment.[87] However, his opinion rests on the interpretation of

[86] See Mitchell, *op. cit.*, 45 (italics added). Clause 3 of the first Financial Agreement provided that the Loan Council should consist of "one Minister of State of the Commonwealth to be appointed in writing from time to time by the Prime Minister of the Commonwealth to represent the Commonwealth, and one Minister of State of each State to be appointed in writing from time to time by the Premier of that State to represent that State."

[87] See Mitchell's interpretation of Clause 3 (a) and (b) of the original Agreement, *op. cit.*, 44:— "The language" (of 3 (a) and 3 (b)) "is inconsistent with the view that a Prime Minister or a Premier can lawfully appoint himself to the Loan Council, to hold office during his own pleasure, even if he happened to be, say, Treasurer as well as Premier. To hold otherwise would be contrary to the natural meaning of the language used . . . " It was to cure this doubt that clause 18 of the 1934 Agreement was inserted; see Agreement relating to Soldier Settlement Loans

the whole of Part I of the Financial Agreement, and hence we believe—especially as the power of appointment may still be exercised by the chief political executives of the Commonwealth and the States—that Sir Edward's conception of the fiduciary position of the Loan Council may still be legitimately examined.

What are the relations of this view to the idea of responsible government? If we paraphrase Sir Edward's view the answer is at once apparent: The function of public borrowing has been removed from the constituent governments of the Commonwealth and vested in an independent statutory body. The members of this body are virtually in the same fiduciary position, and subject to the same rights and liabilities, as if they were a group of appointed public trustees. The implications of their status and functions are inconsistent with any other responsibility than to the "Australian public." Neither the individual parliaments nor their political executives ought to claim any control whatsoever in the exercise of their discretion. To do so, to presume that a member of the Loan Council is acting under the instructions of his Cabinet, that he is advancing the interests of one political unit alone, is inimical to the spirit of the Agreement. If these propositions do not parody Mitchell's view, then the answer to our question is that the Loan Council lies wholly outside the framework of political responsibility. There is no question of deviation from or modification of the doctrine. The principle of responsible government is simply inapplicable.

There would be little difficulty in accepting this fiduciary conception of the Loan Council if Sir Edward had only meant that its members were subject to the general ministerial trust "to serve and in serving to act with fidelity with a singlemindedness for the welfare of the community." In this sense, it would be true of the Loan Council, as of any Minister of the Crown (or member of Parliament), that a submission to coercion or constraint in the exercise of its functions would be a violation of its trust. It is clear, however, that Sir Edward intends much more than this. In his view, the "community" to whom the trust is owed is not the political community organised into its various constitutional units, but the "Australian public." And the remedies of this "public" for the violation of the trust—even if the violation consists of an attempt by a parliament to fetter its representative on the Council by instructions on how to

(confirmed by the federal Parliament by Soldier Settlement Loans (Financial Agreement) Act, No. 26 of 1935) made 3rd July 1934; see (1935) 146 Commonwealth Parliamentary Debates, 1055.

vote—are not "political" remedies, but the full aid of the Courts themselves.[88]

If the Financial Agreement is capable of this novel construction, it is patently clear that neither the original purpose nor the operation of the Loan Council supports this view of its status and obligations. In essence, the purpose of the Loan Council was to rationalise public borrowing by eliminating wasteful competition and by regulating the loan requirements of seven Australian governments. Under the Financial Agreement the Commonwealth and States surrendered the absolute right to borrow "as much as they liked" *for themselves* in exchange for a limited share in two principal decisions—how much money was to be raised by *all* the Australian governments, and what their individual portion would be. There was no intention of vesting this right in any but a ministerial body; and certainly there was no intention that its members should represent any one else but their individual governments. If we discount its origin, however, and simply look at the operation of the Loan Council, Sir Edward Mitchell's view becomes equally untenable. In the first place, the work of the Loan Council represents only a small portion of the business of public borrowing in Australia. The preparation of seven loan programmes is an extensive administrative task. It involves each government in a series of discussions touching almost every level of the executive hierarchy, and before the programme is submitted to the Council it bears the final approval of each Cabinet. In the Council itself, each member presents his case as a statement of governmental policy; and throughout the negotiations he is chiefly concerned to advance this case, and no other. He is not fettered by detailed instructions for the obvious reason that—apart from their futility when decisions may be taken by a majority vote—it is impracticable to do so when the whole direction of the Council, from beginning to end, is to find a compromise between seven claims on the loan market. On the other hand, he is not free to abandon or neglect his State's case, for the reason that he is a member of the executive responsible for the formulation of the State's claim. Each member negotiates therefore within the broad confines of a brief which is essentially flexible and he is subject to one principal fetter—to strike the most favourable bargain for his government. In short, the whole activity of public borrowing is a process of political co-operation between seven governments; and at no stage of this process is there any suggestion that the members of the Loan Council

[88] Mitchell, *op. cit.*, 49.

are a body of men who, once assembled, throw off their separate political identities and assume the role of "trustees" for the Australian public.

If we reject Sir Edward's view of the Council,[89] if the Loan Council operates primarily as a representative political council and not as a body of public trustees, and if each member—irrespective of the binding effect of the Council's decisions—acts in accordance with his general position as a member of a responsible parliamentary executive, is there any sense in which the Loan Council *as a whole* may be deemed to be politically responsible, and if so, to whom?

The idea of responsible government in British communities entails at least two basic institutional implications:— (a) the political executive (Cabinet) is chiefly drawn from members of the majority—whether of one party or of a coalition in the popular assembly, and (b) the executive is accountable to Parliament and ultimately to the electorate. It is obvious, at the outset, that the first of these elements is not readily applicable to the Loan Council since both its representation and operation are essentially "governmental" and not "party." What of accountability? Clearly, if the acid test of political responsibility is the capacity of the electorate—through parliament—to call the executive to account for its stewardship, and if necessary to arrest or correct its policy by expelling it from office, then it lies beyond the power of any single electorate to exact the full obligations of political responsibility from the Loan Council. But does it follow automatically that if the Loan Council is not politically responsible to any one electorate it is not responsible at all? Are we to assume that a representative council composed of the chief political executives of the seven Australian govenments is—as a whole—not politically responsible to anyone for the formulation of loan policy? That the only operative political sanctions are those which the Council imposes on itself? Or that in a single operation lasting for two to three days each year the Commonwealth Prime Minister and the State Premiers cast off the normal conventions of their office? Let us see: In the first place, we have already asserted—contrary to Mitchell's thesis—that neither the origin of the Council nor the assumptions on which it conducts its business question the active link which binds each member to a responsible executive. Furthermore, although the critical decisions in regard to public borrowing have been removed from the floor of each parliament, there is little doubt that each parliament retains the right to discuss and criticise the

[89] See Sir Leo Cussen's criticism of Mitchell's thesis in *Supplement*, 6.

preparation of the government's loan programme, to seek an explanation from the responsible minister on his conduct of the State's case, and—however perversely—"to encompass the downfall of the prime minister or premier, as the case may be, through a vote of censure." In the second place, it is plain that, if no single Parliament can affect Loan Council decisions, *joint or collective* action by the seven parliaments can do so. Given this, when then does the idea of responsible government break down—in the fact that no parliament, despite its unlimited powers of discipline over its representative, can alter a Council decision without the concurrence of six other legislatures? In other words, is the principle of responsible government abandoned because each individual parliament has submitted to the condition that a decision formulated jointly cannot be reversed except by joint action? If this is true for the unitary system of parliamentary government, we believe that the implications of the federal system compel a different view of the matter.

The reasons may be briefly stated. Basic to the various conceptions of the federal state is the division of power between the central and regional governments. By definition, therefore, one of the cardinal principles of parliamentary government in Great Britain—namely the "omnipotent or undisputed supremacy throughout the whole country of the central government" for all purposes[90] must be radically modified—if not altogether rejected—in a system of federal government. In Australia clearly neither the Commonwealth nor the State legislatures conform to the classical tests of parliamentary supremacy; both operate within a limited field of functions and powers. If we can assume furthermore that there is *some*—though not necessarily *exclusive*—correlation between constitutional power and political responsibility, we must infer that—in constitutional theory at least—responsibility is unified and unlimited in Great Britain; while in Australia, responsibility is either absolute, shared, *interdependent,* or even non-existent.[91] The consequences of this view are fairly clear. It means, for example, that if the implementation of certain policies in Australia—such as regional development, soldier settlement, migration, unification of railway gauges, and so on —is dependent on the collaboration of two or more parliaments, then—whether such co-operation is forthcoming or not—the responsibility for this policy rests on these parliaments jointly, and it can only

90 See L. S. Amery, *Thoughts on the Constitution* (1947), 1-3.

91 See generally A. P. Canaway, *The Failure of Federalism in Australia,* c. iv, and next footnote.

be enforced by the collective pressure of their electorates. The normal concept of unitary responsibility is an inadequate guide and principle in these circumstances. It cannot express the implications of such interdependence because it looks to one source of power and responsibility. For this type of case we must resort to some supplementary concept, such as the idea of collective or group responsibility on the part of two or more units of government to explain the precise constitutional relations, and the precise body of people who can exact the obligations of responsibility. Only through such a concept. we suggest, can the conclusions forced on us by applying the unitary idea of responsible government to the Loan Council be avoided, and the political responsibility of the Council to seven Australian electorates made real and meaningful.[92]

92 Needless to say, the difficulty of enforcing responsibility in these circumstances may constitute a serious argument for the supposed "weakness" of responsible government in the federal system. We shall consider this more closely elsewhere. For the moment, however, one comment: In Canaway's examination of the interrelationship between federalism and parliamentary government his whole argument is founded on one hypothesis—the *exclusive* relationship between constitutional power and political responsibility. For him, the measure of legal authority is the measure of parliamentary responsibility. And hence it followed that no government should be held responsible for an act or policy which lay outside its field of power. On the face of it, it is an attractive thesis, for it seems scarcely reasonable, for example, to visit a State government with the maladministration of federal defence policy or the odium of federal bank legislation; conversely, it is in conflict with what Canaway calls "simple justice" to censure or hold federal government responsible for the particular policy of a State. In practice, of course, the Australian electorate is fortunately insensitive to the niceties of Canaway's thesis, and visits the sins of one government on another quite freely. Its justification may be founded on two grounds: First, the practical difficulties of Canaway's view of responsibility are enormous. Indeed, his thesis bears a closer affinity to the law of negligence than *realpolitik*. Carried to its fullest consequences, for example, it would mean that no vote of censure, no motion of want of confidence, could be argued in Parliament unless the Speaker first took steps to ascertain whether the matter complained of fell within the responsibility of the government—an impossible situation. But presuming, even, the right and ability of the Speaker to subject censure motions, or for that matter any criticism of the government, to this test, there can still be no restraint on the electorate's power to oust any government for any reason whatever, however frivolous or irrelevant. No political version of *Re Polemis* exists to limit the electorate's freedom to choose the grounds for the expulsion of one government and the election of another. Secondly, with the growth of national parties, and the steady centralisation of power in Canberra, it is not entirely unreasonable or contrary to simple justice to fix a State government with vicarious responsibility for federal policy where both are of the same political affiliation. Indeed, when the periods of office do not coincide it may be one drastic form of demonstrating disapproval of federal policy by fighting

What of the "federal principle"? How far is this representative public borrowing authority, whose decisions are final and binding on its members, compatible with this principle? Much of the Australian literature on the Loan Council has been generally concerned to show the degree to which the independence of the Commonwealth and States has been affected by the Financial Agreement in alliance with sec. 105A of the Constitution. The arguments are mainly drawn from the exceptional events of the "depression"—the Premiers' Plan and the Lang *affaire*—and the remarks appear to correspond fairly closely in tone and content.

Thus:

> The Financial Agreement meant "a considerable surrender of independence, both on the part of the States and of the Commonwealth. They gave up rights to borrow as much as they liked, when they liked, where they liked, and on such terms as they liked, . . . the Loan Council was, in effect, endowed with the function of regulating the pace of the capital development of the whole country."[93]

Elsewhere:

> "The basis of federation had been the retention by the States of as much independence as was compatible with the surrender of limited powers to the Commonwealth. Now, however, the *Garnishee Case* has demonstrated that under certain conditions the federal government could attach the revenues of a State and paralyse its whole machinery of government. It was therefore no longer possible to pretend that the States were sovereign bodies, exercising untrammelled independence in the spheres of activity allocated to them."[94]

Again, Forgan-Smith, probably the most influential member of the Loan Council in the 30's, remarked:

> "The trend of the operation of the Financial Agreement has been in the direction of undermining the sovereignty of the States. The Agreement itself laid the basis of the unification policy. Financial control is the major power to-day. Under the Financial Agreement, the Loan Council exercises that financial

a State election on federal issues. The manoeuvre is an unavoidable concomitant of party government. Possibly in some circumstances it may work an injustice on "government." We believe, however, that in a system of divided responsibility especially, it is preferable that the scales should be weighted in favour of the electorate.

93 Cowper, *op. cit.*, 126-127.

94 Greenwood, *op. cit.*, 94.

control, and to a very large extent indeed, the operation of that Agreement has been in the direction of establishing unification."[95] These comments suggest at least three distinct matters for consideration—(a) the nature of the fiscal power "surrendered" by each member of the federation; (b) the reality of the rights vested in each member of the Council in exchange for this "surrender"; and (c) the nature of the sanction created by sec.105A of the Constitution. Before we do this, however, we must first glance at our basic referent—the "federal principle."

The formal definition of the federal state presents little difficulty. Professor Wheare has expressed—what is probably the standard conception of—the federal principle in these terms: *"By the federal principle I mean the method of dividing powers so that the general and regional governments are each, within a sphere, co-ordinate and independent."*[96] The precise ingredients of this definition, however, present much more difficulty. In Dicey the formulation of the federal concept is essentially juridical. The terms *co-ordinate*[97] and *independent* simply express a relationship of legal co-equality as distinct from legal subordination. By contrast with non-federal systems of government, the legal power-relationship in the federal state is immune from unilateral change either by the regional governments or the central government. There is no express suggestion in Dicey that the idea of independence involves any more than this.[98] Wheare, however, despite his claim to agreement with the general stock of formal definitions,[99] gives a broader connotation to the terms "co-ordinate and independent." A division of sovereignty which ensures

[95] See Copland and Janes, *op. cit.*, 10.

[96] K. C. Wheare, *Federal Government*, 11 (italics added); cf. Dicey, *Law of the Constitution* (8th ed.), 135-6:— "The principle which . . . shapes every part of the American polity, is that distribution of limited, executive, legislative, and judicial authority among bodies each *co-ordinate with and independent of* the other which . . . is essential to the federal form of government" (italics added).

[97] *Op. cit.*, 167.

[98] The term "independent"—sometimes interchanged with co-ordinate—like the terms "liberty" and "freedom"—excites an almost limitless range of politico-legal, socio-economic ideas, at once so various, and often so vague as to justify almost any meaning. And it is probably here—in the tangled maze of expectations aroused by the differing ideas of the "independence" available to the constituent units of a federal state—as much as any other factor that we may find an explanation for the disappointment, confusion, and recrimination which states, formerly "sovereign", experience in a federal system. Clearly a realistic theory of "independence" for political units in a federal state is no less imperative than a theory of "independence" for individuals in society.

[99] Wheare, *op. cit.*, 15, footnote (2).

only the constitutional equality of the central and regional governments is not enough. Independence is little or nothing if divorced from means; hence if the federal principle "is to operate not merely as a matter of strict law but also in practice, it follows that both general and regional governments must each have under its own independent control financial resources sufficient to perform its exclusive functions. *Each must be financially co-ordinate with the other.*"[100]

The extension of the federal principle to embrace the realities of economic and fiscal power is an important step. Federalism has probably been too much the plaything of jurists. Given the need for financial autonomy, however, we are still left with the crucial question—how can we allocate the financial resources of a federation to guarantee that each unit will have "sufficient to perform its exclusive functions"? The problem of finding a compromise between independence and sufficiency is no less intractable to-day than it was fifty years ago.[101] Thus, for example, if the grant of concurrent taxing power is dictated by the federal principle, how can we ensure that both the general and regional governments can draw independently sufficient for their needs? By imposing quantitative limits on their power? By allowing their taxing powers to interact freely in the hope that a balance will be struck by chance factors? By allocating specific classes of taxes in combination with obligatory grants? Or by erecting some piece of independent machinery to adjust their claims? Whatever method or combination of methods is applied to resolve this dilemma—if it is at all capable of solution—one thing seems crystal clear, that if the general and regional governments are *both* to enjoy the use of concurrent taxing powers, some mutual limitation on their rights is necessary.[102] To suggest otherwise, to argue that the federal principle is inconsistent with any limitations on the power to tax even if the power is used by the general government to preclude

100 *Ibid.* 97 (italics added).

101 See the stimulating survey of the *Financial Aspects of the Constitution* by the late Professor L. F. Giblin in the Symposium, *Federalism in Australia* (1949), 89-108; the Hicks-Phillipson Report on Revenue Allocation in Nigeria, for a valuable comment on the general principles of federal finance, c.v., 45-56; and the papers read by Professor W. A. Mackintosh and H. P. Brown to the seminar on federation organised by the Australian National University, 1951 (see Federalism: An Australian Jubilee Study (1952), 49-70, 80-105).

102 We do not intend to project into federal theory all the elements of the private law doctrine *sic utere tuo ut alienum non laedas.* In a system of government where Commonwealth policy may impose benefits on some units and burdens on others, this is clearly impossible.

the States from the field of income taxation, is to empty the principle of any meaning.

The implications of this view for the Loan Council are fairly self-evident. If the "federal principle" requires that each unit should enjoy a co-ordinate right to borrow, then the problem posed by the special history of Australian borrowing is this: Does the federal principle require that each unit should be free to borrow to the point where the credit of all the units and the stability of the whole economy are seriously threatened? There is little need to emphasise the significance of public borrowing in the fiscal structure of Australian governments, nor the reasons for their tenacious resistance against control. Yet given the interdependence of Commonwealth and State credit, the volume of their demand, and the consequences of competitive and unrestricted borrowing the question, in our view, seems to admit of only one answer. The remaining problem, then, is the question of method. If the regulation and co-ordination of public borrowing is not inconsistent with the federal principle it is clear, nevertheless, that to vest the Commonwealth with *sole* control would infringe this principle. "No government with *arbitrarily* limited borrowing power can be considered autonomous within its own prescribed field." The only device which meets the specifications of the federal principle in these circumstances, therefore, is the joint control through a representative institution.

If we accept the view that as an institution the Loan Council is in accord with the federal principle, what of its operation? Obviously, if the States have exchanged the absolute right to borrow for no more than a *nominal* right to share in the determination of national borrowing policy, or if the Loan Council is simply a facade for a policy arbitrarily imposed by the Commonwealth, it is impossible to maintain the reality of the federal principle. It is here, therefore, that we must attempt to distinguish between form and substance.

In the first place, it is important to note that the operation of the Loan Council is essentially conditioned by the institutional pattern and behaviour of the internal and external loan markets. The Loan Council—like Canute—cannot command the ebb and flow of the capital tide. For this reason, therefore, one must be careful not to exaggerate its importance in delivering the Commonwealth and State governments into the hands of the banks during the 30's. Clearly, there was nothing in the Financial Agreement nor the structure of the Loan Council to prevent the Council's Labour majority in 1930 and 1931 (5:3) from voting itself the most lavish Keynesian public works programme. It is equally manifest, however, that given a united

bank opposition in Australia, the closure of overseas loan markets, and the inability of the Commonwealth government to manipulate credit by legislative means, such a vote would have had no greater practical effect than to stimulate the spirits of its adherents. Nor must we readily assume that in the absence of the Financial Agreement, the Commonwealth and States could have pursued independent economic policies, borrowed freely, and so on; to do so is to underestimate the strength and uniformity of bank pressure.[103] Indeed, in the special conditions of the "depression" it seems that the minimal utility of the Loan Council was to enable the Commonwealth and States to formulate a joint bargain with the banks, and to this extent, equalise the treatment which might have been meted out to them individually.[104]

The question posed by the critical events of the 30's was in effect this: What is the real significance of the Loan Council in an economic emergency where—as Professor Alan Fisher puts it—"decisions about investment rest in the hands of a comparatively small number" of private men?[105] And the answer appears to be that the Loan Council is then no more than *partly* responsible for the direction of borrowing policy. In 1945, however, the problem assumed a different character. The reorganisation of the Commonwealth Bank and the centralisation of credit policy has ensured—for the time at least—a greater harmony between the Australian banking system and the Commonwealth government. But for the States, the problem posed in the 30's by bank pressure now became this: What is the reality of the Loan Council when the control of credit policy is mainly in the hands of its principal member—the Commonwealth? At first sight we might be tempted to find the answer in the syllogism—the 1945 banking legislation vested the Commonwealth with substantive control of credit policy; the Commonwealth is a member of the Loan Council; and therefore, insofar as the Commonwealth is bound by Loan Council decisions, the States have acquired a more effective control

103 See L. F. Giblin, *The Growth of a Central Bank*, 89.

104 See generally, W. R. McLaurin, *Economic Planning in Australia, 1929-1936;* E. O. G. Shann and D. B. Copland, *The Crisis in Australian Finance* and *The Battle of the Plans;* Cowper, *op. cit.*, passim; and C. H. Herbert, *A Loan Council for Canada: The Australian Experience,* (1936) 2 Canadian Journal of Economics and Political Science, 354—especially at 364: "It should be clearly understood that the Loan Council was not responsible for the inception of the Premiers' Plan; it was merely the machinery by which this Plan, which was in effect the condition upon which the banks would continue to lend money to the governments, was carried out."

105 Quoted in Giblin, *op. cit.*, 89.

over public investment. This is clearly, however, a gross over-simplification. It is impossible to minimise—and more to deny—the Commonwealth ascendancy in the Council. It is in a position—as we have already noted—to influence its policy far more comprehensively than "any small number of men" in the community. In law, the Commonwealth is probably bound by the Financial Agreement to arrange for loans voted by the Council. In practice, however, it cannot raise more than the market will yield—a factor so manoeuvrable under the present federal powers that the Commonwealth may become the real determinant of borrowing policy. Is the Council therefore a *nominal* authority? Have the States only the shadow and not the substance of their right to share in the direction of public investment? We believe not. If the May 1952 meeting of the Loan Council is any evidence, it does not appear that the settlement of loan programmes is simply an elaborate annual pageant in which the States indulge their illusions of power. The bargaining—no less than the final compromise—has every appearance of reality, not fiction. If the States negotiate under pressure, there is clearly a point beyond which pressure ceases to be effective, and the revolt may express itself in the 1952 situation where the States overruled the Commonwealth loan estimate by a 6 to 2 vote. While this in itself can scarcely be decisive, it effect must be to compel the Commonwealth to re-examine further possibilities of compromise.

Finally, what of the exceptional powers of enforcement vested in the Commonwealth by sec. 105A of the Constitution? This matter needs little comment. The *Garnishee Case* left virtually no doubts regarding the ambit of sec. 105A.

> "A State may be compelled," writes Cowper, "to carry out any agreement under sec. 105A and, in the process of compulsion, the 'sovereign rights' of the States may be ruthlessly swept aside . . . in the course of enforcing such an agreement, the control of the servants and of the revenues of the State may be taken out of the hands, not only of the government, but even of the Parliament, of the State; and, indeed, in certain circumstances the people of a State might be prevented from having the government they wanted."[106]

Theoretically, we might say that the existence of this power in the Commonwealth conflicts with the pure concept of the federal principle. Yet, given all its fearsome consequences, it seems to us that the presence of this power in the Constitution is far less important than

[106] Cowper, *op. cit.*, 141.

the circumstances of its use. In over twenty years, the coercive force of sec. 105A has been applied *once,* and then only in the abnormal and aggravated circumstances of the Lang default. Clearly the Financial Agreements Enforcement legislation was not an act of arbitrary caprice. The purpose of enforcement was threefold: (a) to reimburse the Commonwealth as quickly as possible for interest payments made on behalf of the defaulting State; (b) to maintain the reality of the Financial Agreement; and (c) to preserve the reputation of Australian credit. There was no intent to undermine the sovereign rights of New South Wales, or for that matter of any other State. The execution against the revenues of a State was unprecedented, but the High Court was not precluded from testing its validity. Once the crisis had passed, moreover, the legislation ceased to have further effect. If these circumstances suggest the real pre-conditions to the use of this power, then for practical purposes the effect on State rights is negligible.

In a sense we may say that the Financial Agreements Enforcement Act raised precisely the same issues for the federal principle as the National Security regulations raise for the concept of individual liberty in a time of national emergency. The nature of these parallel issues is familiar to students of jurisprudence and political theory. In both cases we are faced with a problem of theoretical consistency and practical justification. In both cases the answers rest on two things: First, on our criteria of liberty for the subject and of independence for the individual unit of a federal state; and secondly, on our evaluation of the circumstances in which the relevant power has been exercised.[107]

In regard to the general influence of sec. 105A on the normal operation of the Loan Council we are simply confronted with another

[107] In *The Case of the People of Western Australia,* the State argued that sec. 105A was "a power in the hands of the Commonwealth which definitely attacks and undermines the sovereign and independent rights of the States as self-governing communities" (at 91). Quite apart from any other objections to the use of the term "sovereign"—a concept of misleading associations and entirely out of place as a juridical description of an Australian State—one can have some sympathy with the Commonwealth reply. "It is absurd to suggest that this legislation passed to compel a defaulting Government to fulfil its obligations under the Agreement, "attacks and undermines" the constitutional rights of the States. It might just as well be said that the policeman on his beat "attacks and undermines" the liberty of the citizen. All that is put forward in the *Case* in this connection amounts to no more than a vague and formless fear of something that may possibly happen, but which never would happen except in extraordinary circumstances" (*The Case for Union,* 24).

version of the traditional problem of "law and the sources of obedience." We need not enter this prickly thicket. It is enough to say that if the Austinian policeman lurks in the apparel of sec. 105A, his influence is less obvious than the material self-interest of the Commonwealth and States in the continued operation of the Loan Council. Indeed, it is probably decisive that in the twenty-three years of its life few, if any, of the Council's severest critics have suggested a return to independent borrowing.

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