Geographical inequalities and sub-national funding in Australia

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Figure 1- Image by Patty Jansen from Pixabay

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Context

This case study is the result of a review of intergovernmental transfers and other sub-national funding in Australia and to what extent these funding streams are designed and able to reduce geographical inequalities. The aim of this review is to draw out lessons for England, and the UK more broadly, in terms of how funding mechanisms can be used to better address spatial inequalities. The review is mostly based on desk research of academic and policy publications, complemented by interviews with several key informants in Australia, including academic experts and policymakers at the federal and state level.[1]

The reason for conducting a case study of funding mechanisms and geographical inequalities in Australia is to be able to compare the UK to a more decentralised country with a federal constitution, in which federated states and territories retain substantial powers and competencies. With the UK, and particularly England having undergone – and continuing to undergo – progressive devolution of policy areas to the (city-)regional scale, the Australian case offers insights into the functioning of a multilevel governance system that is considerably more decentralised than the UK. Moreover, despite the existence of spatial inequalities in Australia, it is often considered to have a fairly successful model for maintaining relative fiscal equality between states (Dougherty and Foreman, 2021).

This paper provides a selective review of issues most relevant to the English context: the extent and nature of geographical inequalities in Australia and policies addressing geographic inequalities and regional development (section 2), the Australian system of governance and its recent history (section 3), and funding for state and local government in Australia, including tax-raising powers, fiscal transfers and grants, and the balance of accountability and devolved policy discretion afforded by these funding streams (section 4). Other topics central to Australian debates, such as policies and funding aimed at Indigenous communities, are less emphasised as they are less applicable to the English context.

Australian debates about geographic inequalities

Australia is the sixth largest country in the world by land mass and is currently the world's 13th largest national economy. The nation of Australia was created in 1901 when six British colonies - New South Wales, Victoria, Queensland, South Australia, Western Australia and Tasmania - united to form the Commonwealth of Australia. In 1911, the

[1] In addition, the author would like to thank Andy Pike, Anne Green, Charlotte Hoole, and especially Sally Weller for their valuable feedback on this case study.

Northern Territory was separated from South Australia, and the Australian Capital Territory from New South Wales, creating the six states and two territories that make up the nation today. Australia is a federation, with the states and territories (henceforth 'states') retaining a fairly extensive set of capabilities and responsibilities – though ever since the early twentieth century there has been a gradual centralisation of power and control (Stewart, 2023).

Geographic inequalities in Australia and how they are understood

Australian public debates on inequalities have over recent years mostly centred around inequalities between ethnic groups (non-Indigenous Australians versus Indigenous communities) as well as about Lesbian, Gay, Bisexual, Transgender, and Intersex (LGBTI) and disability issues, rather than spatial inequalities. Nonetheless, geographic inequalities do exist.

Similar to how geographic inequalities in England can be divided into inequalities between regions and within regions, geographic disparities in Australia can be seen as a combination of inequalities between states and inequalities within states. On the between-state level, a division exists between the more urbanised and densely populated states of New South Wales, Victoria and Queensland, and the remaining states and territories which are more sparsely populated. A further division can be made between the resource-rich states of Western Australia and Queensland which over the past two decades have seen strong economic growth based largely on mining exports, and the remaining states and territories in which growth in economic output has been more modest. Tasmania in particular has a comparatively weak economy with little private investment.

Within states there is often a pronounced divide between the major metropolitan areas on the one hand and non-metropolitan areas on the other (Pritchard and McManus, 2000; Haslam McKenzie, 2024). The former, particularly the state capitals, have seen strong services-led economic growth over recent decades as well as robust population growth (Infrastructure Australia, 2010; McGuirk and Argent, 2011; Weller and O'Neill, 2014). The latter are often referred to with the label 'rural and regional Australia', and large parts of this category – though not all – have been affected for several decades by depopulation and lacklustre employment growth (Australian Bureau of Statistics, 2023b; Gray and Lawrence, 2001; McGuirk and Argent, 2011; Mitchell and Carlson, 2005; Pritchard and McManus, 2000). However, several 'regional centres', i.e. medium-sized cities within non-metropolitan Australia, have seen relatively healthy population growth rates in recent years (Li et al., 2024).

To the extent that Australia has seen debate about geographic inequalities over recent decades, this has primarily revolved around the need to support or strengthen 'rural and regional Australia'. In other words, the main emphasis has been on intra-state inequalities, with disparities between the states and territories receiving somewhat less attention – though this is not entirely absent. This could in part be seen as a consequence of relatively strong fiscal equalisation between the states which ensures a relatively equal provision of key public services and infrastructure (see section **Error! Reference source not found.**). States have responsibility over many functions and areas of service delivery close to people's day-to-day lives, for instance schools and hospitals.

Geographic disparities between metropolitan and 'rural and regional' Australia are demographic in nature as much as economic. Australia has a very uneven population distribution, and many rural and regional areas have very low population densities. This poses challenges for service delivery and infrastructure provision, which have in many cases been compounded in recent decades due to population shrinkage in remote areas of Australia (Australian Bureau of Statistics, 2023b; Haslam McKenzie, 2024). In contrast, large metropolitan areas have tended to see substantial population growth over recent decades – to an important extent driven by immigration – and account for an ever-increasing proportion of the Australian population (Australian Bureau of Statistics, 2022; Hamnett and Maginn, 2016). But economic differences exist across the metropolitan-regional divide, too. For instance, many of the more remote and rural areas of Australia have strongly agricultural or natural resource-based economies, whereas the economy is more service-oriented in urban areas. On the whole, urbanised areas in Australia also tend to have seen faster economic and employment growth over recent decades (DITRDCA, 2022; Infrastructure Australia, 2010).

But there are important caveats to this simplistic picture of an urban-rural divide. For one, there are important economic variations within urbanised Australia. Like other mature industrialised countries, Australia has been affected by manufacturing decline over the past several decades. In particular, during the 1970s, 1980s, 1990s, and 2000s there have been whole industry closures in all trade-exposed sectors including the automotive sector (General Motors, Mitsubishi, Ford Australia, Blackstone Tyres) and the textiles clothing and footwear sector, as well as a major contraction of the steel industry. Deindustrialisation has had a disproportionate impact on the cities and suburbs that were formerly home to these industries, for instance Geelong in Victoria (Tierney et al., 2024). While some cities, such as Sydney, were able to compensate for the loss of manufacturing employment by expanding into new sectors like financial and business services and IT, other areas were less able to do so (Beer, 2012). The decline of manufacturing industries has been met by a policy response in the form of structural adjustment programmes which have often been both geographically and sectionally targeted (see section 0).

Another, rather unique, factor that has a substantial impact on the economic geography of Australia is its large mining sector. Since the early 2000s in particular, the country has experienced a mining boom fuelled by high demand for energy and iron from China. This has led to a substantial economic and employment boost to resource-rich rural parts of Western Australia (home to large iron ore deposits) and Queensland (the same but for coal), and to a lesser extent the Northern Territory and New South Wales (Connolly and Orsmond, 2011; Fleming and Measham, 2015; Nicholls and Rosewall, 2015). Because these activities are coordinated from the cities and tend to use a 'fly-in-fly-out' workforces, and because the firms are transnational with few local allegiances, resource-intensity brings benefits to the state capitals but does not translate into a stronger economic position locally (Ellem, 2022).[2] The mining boom gave rise to debates about a 'two-speed economy' during the late 2000s and early 2010s, with mining states forging ahead while much of the rest of the country languished (Mitchell and Bill, 2006; Perlich, 2013; Rourke, 2012). Since the early 2010s, mining output has contracted somewhat amidst reduced demand from China, but remains very substantial (Foo and Salim, 2022). In 2021-22, the mining industry contributed $42.2bn in company tax to the national budget (in addition to royalties paid to state and territory governments) (Australian Taxation Office, 2024), equivalent to 22% of the $186.2bn national welfare budget (AIHW, 2023). Therefore, mining plays an important role in mitigating inequality in urban areas.

National policy on geographic inequalities and regional development

In part, geographic inequalities are addressed through fiscal equalisation mechanisms operating within state (and, to an extent, local) funding. These are described in more detail in section 4.

Aside from this, Australia has policies aimed at fostering regional (economic) development. Responsibility for regional development mainly lies with the states, with the national Government having a more limited role in this policy area (Weller and Beer, 2023).[3] However, the Federal Government has played an increasing role in regional policy over recent decades.

While very little central government policy was dedicated to regional development during the latter part of the twentieth century (apart from the short-lived existence of the Department of Urban and Regional Development (DURD) in the 1970s), this began to change under Paul Keating's Labor Government of the early 1990s. This was in part because of a turn towards market-led policies during the 1980s, which involved the opening of the economy to global forces and a reduction in state investment in service delivery and infrastructure in rural and remote communities (Gray and Lawrence, 2001; O'Neill and Fagan, 2006). These impacts increased spatial and social inequalities and

[2] A large portion of the benefits of the mining boom flow to urban areas through urban-based mining service providers and long-distance 'fly-in-fly-out' workers (Haslam McKenzie, 2024).

[3] Though there is substantial *de facto* redistribution of federal resources to peripheral regions in the form of social security and state-funded social services.

contributed to "economic and social upheaval" in adversely impacted locations (Haslam McKenzie, 2024; Tonts et al., 2005). The main policy focus during this time was on specific neighbourhoods that had been affected by structural change. A Taskforce on Regional Development led to the establishment of Regional Development Organizations (RDOs), though funding for these was very limited and their role was advisory only (Tonts et al., 2005).

Voter dissatisfaction led to the reinstatement of a Liberal Party-National Party coalition Government in 1996, which terminated all regional development programmes and many social support programmes. Federal spatial policy returned to a narrower emphasis on providing the states with funds to essential infrastructure like roads and telecommunications. [4] During this time, however, increasing signs of disaffection emerged in many rural and traditional industrial areas, fuelling minority political parties. An outcome was the electoral success of the right-wing populist One Nation party, which advocated curbing migration and increasing support for small business in rural and deindustrialised areas. This disaffection led to the election of independent and minor party representatives in both Federal and state parliaments. Since Australia has a two-party political system with often fairly small differences between the major parties, governments are often forced to make concessions to buy the support of independents (Interview, academic). Consequently, the electoral dissatisfaction translated into a shift in policy across all parties towards recognising the challenges of 'rural and regional Australia'.[5]

One result of this was the establishment in 2008 of the Regional Development Australia (RDA) programme, building on the previously-established Area Consultative Committees (Buultjens et al., 2012). RDA currently consists of a network of 53 regional committees that work to support economic development in the regions (RDA, 2023). Because the Federal Government is constitutionally prohibited from interfering directly in state matters, these committees are set up as partnerships between the national, state, territory, and local governments, and operate across geographies that do not map directly onto local government boundaries. RDA committee members are usually drawn from the business communities of their region (Buultjens et al., 2012). The committees develop Regional Strategic Plans that identify projects to stimulate and increase the competitiveness of local businesses or support entrepreneurship. However, RDA committees have no power to implement, and few resources compared to state-level institutions involved in regional policy (Weller and Beer, 2023). Their effect, in practice, is to align state and Federal priorities. An important role for the committees is to feed in local intelligence into central government to help guide government policies. At times

[4] Ironically, it was an MP from the National Party, traditionally the party of rural Australia, who formally abandoned these regional development policies (Tonts et al., 2005). Coalition policy insists that regional development is a state not a federal responsibility.
[5] See Weller (2023) for detail on the political landscape.

RDA committees have had an uneasy relationship with state-funded regional development organisations (Interview, academic).

In 2023 the Australian Government set out a new Regional Investment Framework (DITRDCA, 2023) to guide their wide-ranging array of initiatives and programmes targeted at regional Australia. For more detail on regional development funding see section 0.

A further national policy area with spatial impacts are structural adjustment programmes designed to mitigate the negative effects of declining industries and support individuals and communities affected by such decline to move into new economic activities. While not explicitly framed as spatial policy, because of their often spatially-targeted nature (towards areas affected by the closure or shrinkage of particular sectors) these programmes often act as a *de facto* regional policy (Beer, 2015). Over the period 2000–12, more than $88 billion worth of structural adjustment packages was invested by the Australian Government in areas affected by the shrinkage or closure of industries (Beer, 2015). Structural adjustment programmes were introduced during the Hawke administration (1983-88) to buy the support of organised labour for structural change. They still operate on a wide scale today.

A final emerging area of (implicit) spatial policy is that around energy transition. Though Australia has arguably been hesitant to adopt stringent and ambitious decarbonisation policies due to its reliance on the extraction and export of fossil fuels (Leandro, 2023), recent years have seen the start of a cautious debate about the future of the resource economy and the communities which rely on it. Aside from a brief period of carbon pricing from 2012 to 2014[6], Australian energy transition policies over the last 10-15 years have mainly been in the form of financial support for new technologies like solar and wind energy (Geroe, 2022). Geographic areas with abundant solar, hydro, and wind resources would seem likely beneficiaries of such policies. The Australian Government has recently announced a $23bn investment package to support the growth of renewable energy, 'green' manufacturing, and other strategic economic sectors (Australian Government, 2024a). The spatial impacts of this policy are not yet clear, but the policy is in part framed as a way of securing the economic future of (fossil-fuel reliant) Western Australia and the Northern Territory (Albanese, 2024; King et al., 2024).

Governance and history

Australia has a federal system of government in which the Federal Government has powers and responsibilities over certain policy areas, and the states and territories have responsibilities over others. The respective responsibilities of the federal, and state and

[6] This was introduced by the Labor government under Gillard but repealed by the Liberal–National Coalition government under Abbott.

territory governments, are agreed through national agreements (see section 0 for more detail). Australia's federal relations framework includes intergovernmental forums for Commonwealth, state, and territory ministers to address priority cross-jurisdictional issues. At its core is the National Cabinet, established on 13 March 2020, comprising the Prime Minister and state and territory First Ministers. The precursor to the National Cabinet was the Council of Australian Governments (COAG), which was established in 1992 and was instrumental in facilitating better state-federal cooperation. Local government does not exist in the federal constitution so local government powers and responsibilities are defined in state law. An overview of the three levels of government, with a particular focus on intergovernmental financial relations, is provided in section 0. But first, section 0 provides a brief historical overview of fiscal federalism in Australia.

A brief history of fiscal federalism in Australia

Fiscal transfers from the Federal Government to lower levels of government have been present since the inception of the Australian Federation in 1901, and have been subject to various reforms over the past 120 years. To an important degree, the establishment of fiscal transfers was a response to the Federal Government's gradual curtailment of the ability of states and local government to raise their own revenue (Fenna, 2008).

Fiscal transfers from the Federal Government to the states were instituted as part of the Australian Constitution that set out the terms of the Federation of Australia out of the previously independent colonies. Federation resulted in the removal of all duties on trade between the states, which had previously been a major source of state (colony) revenue. The Federal Government, which assumed all power to raise duties and excise, was as a result left with a substantial surplus revenue while the states were in a deficit, and as such an arrangement was made for most of the surplus revenue to be returned to the states (Burton et al., 2002; Fenna, 2008). When, in 1942, the Commonwealth additionally assumed the sole ability to raise income tax[7], a system of reimbursement was introduced to compensate the states for their loss of income tax-raising powers and revenue (Burton et al., 2002; Nicholas, 2003). This increased both the scale of vertical fiscal imbalance and fiscal transfers to the states considerably. From 1959, these transfers were no longer called 'reimbursements' but were instead relabelled 'financial assistance', an implicit move away from recognising these payments as compensation for the Commonwealth having curtailed states' ability to fund their own activities (Fenna, 2008). This change can be seen as cementing and formalising a relationship of increasing dominance of the Federal Government over the states (Parkin and Anderson, 2007; Stewart, 2023).

[7] This was initially intended to be a temporary arrangement for the duration of WWII only, but was subsequently extended indefinitely (Burton et al., 2002).

During the 1960s and 1970s, the Federal Government began to distribute an increasing share of fiscal transfers to the state level via 'specific purpose grants' (Spahn and Shah, 1995). These are grants which, unlike the financial assistance payments described above, are required to be spent on specific national policy objectives. The increased use of these conditional grants led to accusations that "...the states are more and more becoming the administrative spending agencies of the Federal Government" (Burton et al., 2002). Though the reliance on specific purpose grants has fluctuated over time with successive governments, the overall trend has been in favour of a growing reliance on these conditional grants over time. For instance, in the financial year 2003/4, specific purpose payments made up 40.6% of overall payments to the states, but in 2024/5 they had increased to 49.2% of total payments (Australian Government, 2003, 2024b).[8] Similarly, the States' funding to local government is also increasingly tied to specific policy requirements.

In the late 1990s, following a High Court decision, the Federal Government assumed all rights to impose sales tax (prior to this date states had levied sales taxes on tobacco, alcohol, and petrol). Subsequently, a major tax reform in 2000 saw the Federal Government impose a new Goods and Services Tax (GST)[9] which was, and continues to be, redistributed in full to the states (Parkin and Anderson, 2007). Although generally seen as strengthening the financial position of the states, this reform could at the same time be argued to have further shifted tax-raising powers away from the state level and towards the Federal Government, since, in exchange for the new GST payments, the states were required to abolish or reduce several state taxes (Burton et al., 2002; Parkin and Anderson, 2007). However, on a more positive note, the GST revenue is awarded in the form of 'general purpose' or 'untied' grants which states are free to spend in whatever way they see fit, and as such allows them to preserve a degree of policy freedom.

Responsibilities and tax-raising powers of the different levels of government

The Federal Government is based in Canberra. It is responsible for international and inter-state matters including monetary policy, defence, immigration, post, telephone and internet services, higher education, and social security – which includes pensions, out-of-work and incapacity benefits, and childcare and elderly care subsidies. The Federal

[8] In 2003/4, specific purpose payments to states and territories (including payments through states and direct to local government) totalled $18,456 and general revenue payments (GST plus other general revenue assistance) totalled $25,566 (Australian Government, 2003, p. 67). In 2024/5, specific purpose payments to states and territories (including payments through states and direct to local government) totalled $91,159 and general revenue payments (GST plus other general revenue assistance) totalled $94,411 (Australian Government, 2024b, p. 7).

[9] This is essentially a value-added tax.

Government also administers the state healthcare insurance system Medicare, with healthcare services being delivered by state and territory governments in an extensively privatised but nonetheless government-dependent system of provision.[10]

States and territories are responsible for within-state matters, including many day-to-day and essential public services including primary and secondary schools, hospitals, provision of residential elderly care and childcare, child protection, policing, and public transport (Nicholas, 2003), as well as being traditionally the main level of government responsible for regional development policy.

Lastly, local government consists of over 550 local councils, which are generally responsible for waste collection, leisure (which includes libraries and public parks), parking, local roads, public health, community services, and some childcare and elderly care services. The actual functions of local governments vary from state to state, and within states depending on the size and policy choices of local councils. Relatively few local government services are statutory, most are discretionary (Law Handbook, 2016).

The Federal Government has the most extensive tax-raising powers, including the ability to raise income tax[11], customs and excise duties, company income tax, and sales tax. The tax-raising powers of the state and local levels are much more limited. The states are able to raise payroll taxes, land tax, gambling taxes, and taxes on insurance.[12] The mining states also derive significant funds from mining companies, in royalties and other payments. In Western Australia, these funds are redistributed to the regions. Local government's sole source of income is municipal rates, and in addition they have the power to levy certain charges and raise revenue through the sale of goods and services (OECD, 2024). In some states (e.g. NSW) local government collects royalties for mining and extraction land uses.

The Federal Government currently raises about 82% of total tax revenue in Australia, with states raising just over 15% and local government raising just under 2% (Australian Bureau of Statistics, 2024b). The limited tax-raising powers of states and local councils mean they are unable to raise sufficient revenue to meet their responsibilities, which, in the case of states, are substantial.[13] This necessitates the transfer of centrally-raised revenues to the states and local governments. The Federal Government controls the vast majority of tax revenue, but is responsible for only around half of government service delivery in monetary terms, creating a high degree of vertical fiscal imbalance (Fenna, 2008). This fiscal imbalance is both a consequence of the increasing centralisation that

[10] General practitioners are generally private businesses.

[11] The Commonwealth has had the sole right to levy income taxes since 1942.

[12] Value-added tax (Goods and Services Tax) is raised centrally by the Commonwealth but remitted to the states.

[13] Though it is important to note that state responsibilities are not unilaterally imposed by the federal government but agreed in bilateral agreements.

has taken place in the Australian Federation since its inception, as well as an instrument for further extension of central policy control (Eccleston and Krever, 2017; Fenna, 2019).

Governance at the local level

Unlike states and territories which have defined constitutional powers and responsibilities, local government does not exist in the Australian constitution, with local government functions and jurisdictions defined at the state level. Despite some variations, local government functions are limited compared with those of local authorities in England. With Australia having a federal governance system, states have substantial power over local governments, having the ability to impose regulatory, structural, and financial changes when they see fit, often in response to perceived local government failings (Sansom, 2020). There is considerable variation between states in the degree of local autonomy and authority of local government.

Local government areas are typically governed by an elected council, and usually have a mayor or shire president who presides over council meetings. Mayors are either directly elected, or elected by the board of fellow councillors. Australian local government has traditionally followed a managerial framework where a few elected councillors act as a strategic board of directors, focusing on policy while daily operations are managed by the chief executive. However, recent legislative changes in several states have clarified roles and responsibilities, enhancing the democratic role of elected officials and to some extent shifting power away from management (Sansom, 2020).

Australia has a long history of local government reform, but particularly during the period 1990-2016 there has been forced local government consolidation in most states. Tasmania (1990-1995), Victoria (1995-2007), Queensland (2007), South Australia (1995-1998), and the Northern Territory (2008) have all witnessed extensive restructuring in recent decades, motivated by increasing cost pressures and financial sustainability concerns in local government (Dollery et al., 2013). New South Wales underwent local government amalgamation during the 1970s and early 1980s (Tiley and Dollery, 2010), and in 2011 embarked on a sweeping forced amalgamation process which proved sufficiently controversial that it was halted in 2017 (Dollery and Piper, 2020).[14] Western Australia is the only state in which local government has over the last several decades not been subject to forced amalgamation. This consolidation/ amalgamation resulted in a stark reduction in the number of local government areas in each state. For instance, between 1990 and 2000, the number of local councils in Victoria went from 210 to 78, and in the Northern Territory from 69 to just 16 (Aulich et al., 2011). Nonetheless, with an average population of 48,543 in 2023 (Australian Bureau of Statistics, 2023a), Australian

[14] The newly elected NSW Labor government introduced a bill in early 2024 to allow local councils to de-merge, which was passed in May 2024 (OLG, 2024).

local government areas remain small compared to the UK (where the average population of district councils is around 115,000 (Sandford, 2022)). Moreover, there is a long tail of very small local authorities. In 2023, there were 236 local government areas with a population of less than 10,000, out of 539 total local government areas (Australian Bureau of Statistics, 2023a), though some of these areas have a geographical footprint as large as Wales.

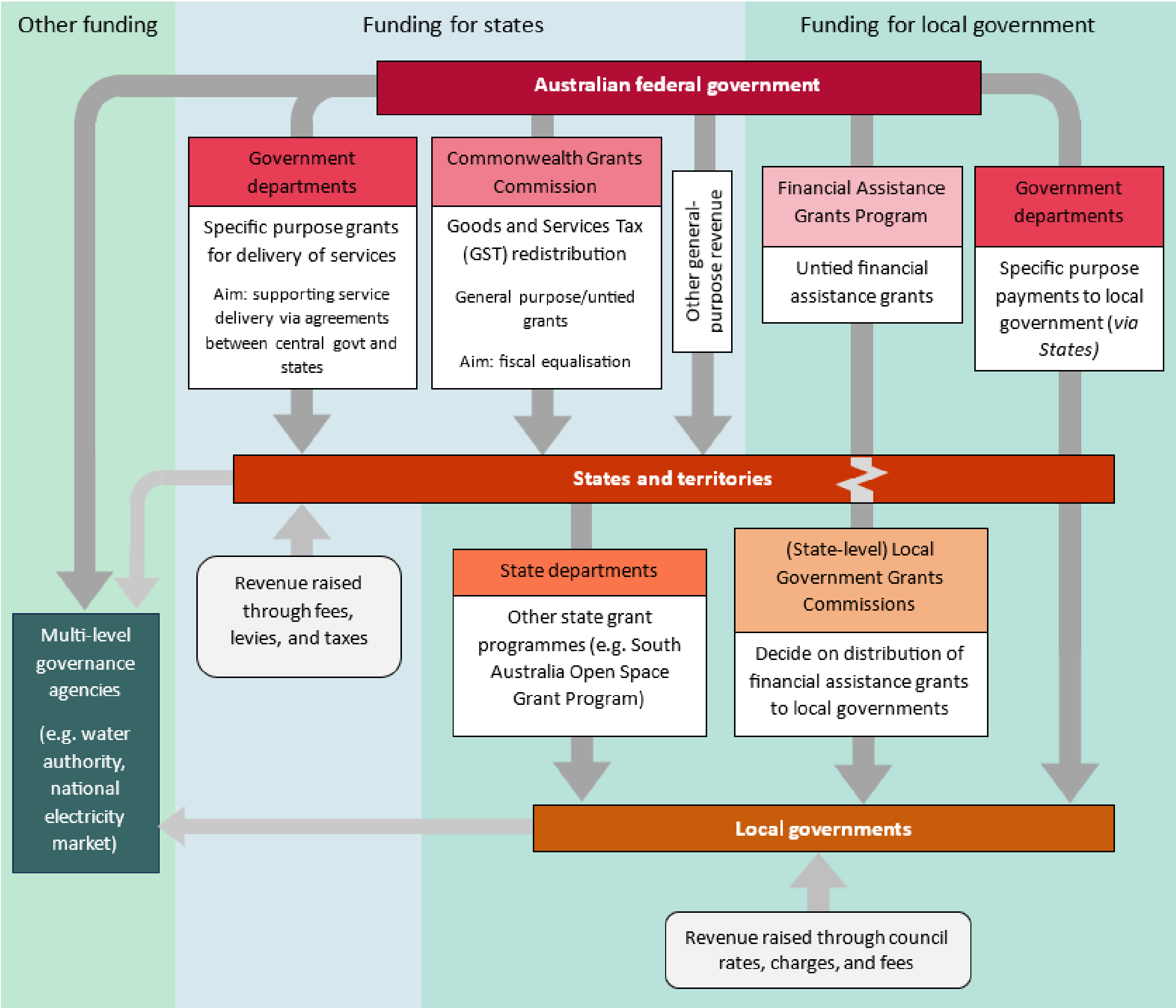
State governments often cited inefficient local use of resources and lack of capacity as reasons for forced local government amalgamation and other forms of restructuring. However, these shortcomings have been argued to at least in part be the result of the instability of local government revenue in a context of very high dependence on fluctuating state- and federal grants (Michel & Taylor, 2012). This funding instability has hampered the ability of local councils to plan for and deliver consistent services or achieve capacity to win additional funding (ibid.). In addition, the fiscal sustainability position of local governments has also been affected by the expanded remit and responsibilities of Australian local councils over recent decades, which have not been matched by concomitant increases in financial capacity (Australian Local Government Association, n.d.; Brackertz, 2013).

Funding systems issues: allocation, delivery, local tax raising, monitoring and evaluation

The following two sub-sections describe the main intergovernmental fiscal transfers in Australia, alongside other forms of state and local government revenue – focusing first on sources of funding at the state level, followed by sources of funding at the local government level.

Figure 1 provides an overview of the main funding streams between the federal, state, and local level. This is by no means complete but intended to serve as a visual aid.

Figure 1: Schematic representation of main intergovernmental funding streams in Australia



Source: Author's own figure based on literature cited throughout section 4. Thicker arrows represent flows of funding, thinner arrows represent influence and/or control over governance and funding decisions.

Funding for states

States raise a proportion of their revenue themselves, through:

- Payroll taxes
- Taxes on property transactions
- Land taxes
- Mining royalties
- Other levies and charges, such as on gambling

They also receive a substantial proportion of their income through fiscal transfers from the Federal Government, about 45% on average (though this varies considerably across states). These transfers come in two main forms:

- Specific purpose payments
- General revenue assistance (mainly GST revenue)

Specific purpose payments

Specific purpose payments (SPPs), also referred to as 'tied grants', are ringfenced for specific policy areas, such as for education or health. SPPs can be seen as a "means of promoting national standards and setting strategic directions in a federation" (Nicholas, 2003), or, in a more critical interpretation, as a way for the national Government to impose its policy aims on the states and territories (Fenna, 2008). SPPs can be broadly divided into recurrent funding (i.e. funding to cover core, continuous costs of providing services), and programme-specific funding. This model leaves room for State-level differences in implementation, which in turn allows innovation to create competition among the States and enabled best practice options to emerge and become institutionalised nationally.

Recurrent specific purpose payments to states

Prior to 2008, conditions for recurrent specific purpose payments were set out in over 90 separate funding agreements (Koutsogeorgopoulou and Tuske, 2015). Through the Intergovernmental Agreement on Federal Financial Relations (Commonwealth of Australia, 2008), these were consolidated into broader National Agreements setting out the aims and priorities in different policy areas, the responsibilities of both the federal and state governments, and payments to be made to the states to fulfil these responsibilities. This change has been welcomed for improving the clarity of state funding arrangements, and reducing the conditionality of state funding by tying payments to broad shared objectives while allowing states a degree of flexibility in how to meet these objectives (Koutsogeorgopoulou and Tuske, 2015).

Currently there are five National Agreements, covering schools, health, mental health and suicide prevention, skills, and social housing and homelessness. Taking schools as a first example, under the National School Reform Agreement (COAG, 2019) the Commonwealth provides 20% of total recurrent funding for government schools and 80% of total recurrent funding for non-government schools[15], with the remainder to be

[15] The Commonwealth share of recurrent school funding is not technically paid to states, but instead to schools directly. However, this funding makes an important contribution to state education services.

provided by state governments and/or parental or private contributions (DoE, 2024a). The Commonwealth share of school funding is allocated according to a formula which sets out a base amount per student, which is weighted for factors including disability, Indigenous background, socio-educational disadvantage, non-English-speaking households, as well as remoteness and school size (DoE, 2024b; Government of Australia, 2013). For non-government schools, the school community's 'capacity to contribute' is also taken into account, based on the median family income of students at the school (DoE, 2024c). Due to these weightings, schools in some states receive more federal funding per capita than others, with the Northern Territory receiving the highest per capita amount (Australian Government, 2024b) owing to the remoteness of many of its communities and a significant Indigenous population.

Another significant area of recurrent funding is federal support for public hospital services provided by the states. The current terms are set out in the 2020-25 National Health Reform Agreement (DHAC, 2024). States receive two types of hospital funding: activity-based funding and block funding, of which activity-based funding is the largest proportion (NHFB, 2024). Activity-based funding is calculated based on the number and types of services provided to patients in each state (e.g. emergency services, acute admitted hospital services, non-acute hospital services) and the cost of delivering those services. Activity-based funding is thus allocated on the basis of need in terms of actual service delivery, and as such the amount of per capita funding differs between states (NHFB, 2024).[16] States receive block funding for teaching, training and research, public health programmes, and public hospital services in settings where block funding is more appropriate like small rural hospitals (NHFB, n.d.).

Non-recurrent specific purpose payments to states

In addition to recurrent funding, the Federal Government also provides specific purpose payments to states for specific (time-limited) programmes or policy reforms. These have recently been brought together under multilateral Federation Funding Agreements covering five service sectors: health, education and skills, infrastructure, environment, and affordable housing and community services (Federal Financial Relations, n.d.). These agreements set out the funding states will receive to support the delivery of specified initiatives, which can be either nation-wide programmes like the BreastScreen Australia Program, or state-specific initiatives such as the Western Australian Hospital Infrastructure Package (Federal Financial Relations, 2020a) and the Northern Territory Remote Aboriginal Investment programme (Federal Financial Relations, 2024b).[17]

[16] The Northern Territory again receives the highest amount of per capita funding.
[17] These are just a few examples of the dozens of such programmes that exist under the five Federation Funding Agreements.

Funding formulae for nation-wide programmes vary, sometimes being allocated based on population or the number of service users across states (e.g. for the Housing Support Scheme (Federal Financial Relations, 2024a) and some health-related funding (Federal Financial Relations, 2020a), sometimes taking into account measures of need (e.g. in the case of the Schools Upgrade Fund (Federal Financial Relations, 2020b).

General revenue assistance

General revenue assistance, unlike SPPs, can be spent on any purpose. It is for the most part made up of centrally-raised GST revenue that is remitted to the states. Unlike SPPs, a key stated goal of these payments is to provide fiscal equalisation between the states, by accounting for the uneven capacity of states to raise revenue and uneven costs of delivering services. The distribution of GST revenue is decided by the Commonwealth Grants Commission.[18] This commission uses an equalisation principle to guide its approach, which, since 2010, has read as follows: "State governments should receive funding from the pool of goods and services tax revenue such that, after allowing for material factors affecting revenues and expenditures, each would have the fiscal capacity to provide services and the associated infrastructure at the same standard, if each made the same effort to raise revenue from its own sources and operated at the same level of efficiency" (Commonwealth Grants Commission, 2017).

The approach to horizontal equalization applied by the commission has been described as comprehensive, involving detailed calculations to account for differences in the costs of providing services, states' revenue-raising capacity, and differences in the inter-state allocation of specific purpose payments (Nicholas, 2003). Importantly, the commission emphasises that while states should have an equal capacity to provide services, they aim to preserve "policy neutrality", in the sense that the equalisation principle should not provide an incentive or disincentive for the states to alter their own revenue-raising choices. For instance, there should not be an incentive for states to reduce the amount of payroll tax or land tax they collect locally in the anticipation that this shortfall will be made up by an increased receipt of GST revenue (Commonwealth Grants Commission, 2017).

The Commonwealth Grant Commission assesses the revenue-raising capacity of each state (under the assumption of equivalent taxation policies), and the expenditure required for each state to provide an equivalent level of services and infrastructure. Factors taken into account in these assessments include states' property prices (which affect the amount of conveyancing and land tax states are able to raise), employment

[18] Technically the Commonwealth Grants Commission only advises on the distribution and the relevant Treasury Minister makes the actual decision, but in practice the advice of the grants commission is always followed.

and wage levels (which affect the amount of revenue that can be raised through payroll taxes), and the value of mining production (which affect the ability to raise revenue from mining royalties). Factors considered to affect the cost of providing services and infrastructure include the demographic and socio-economic composition of the population, population dispersion and density (since a more dispersed population implies greater transport-related costs and increased costs of service provision), and population growth (Commonwealth Grants Commission, 2024). Prior to 2018, GST funding was allocated such that, including the GST, total assessed revenue for each state equalled assessed expenditure, resulting in equal fiscal capacity across states.

The states which have benefitted most from this principle, in the sense of receiving a significantly higher share of general revenue assistance than their share of the GST tax base, are the Northern Territory, Tasmania, and South Australia. The Northern Territory has in recent years received around five times as much revenue assistance than the amount of GST raised locally (largely because its assessed expenditure needs are much higher than those of other states), and Tasmania and South Australia have received around 1.9 and 1.5 times as much as their local GST tax base (Commonwealth Grants Commission, 2024). The application of the HFE principle therefore produces a substantial amount of territorial redistribution towards more peripheral and less-populated states.

Since 2018, however, a new distribution arrangement has been in place as a result of dissatisfaction expressed by Western Australia that it received less than its 'fair share' of GST revenue. Western Australia has a much stronger revenue base than other states due to its mining royalties, so due to the redistributive nature of the GST system, the amount of GST revenue it receives is far less than the amount of GST raised in the state. It has consequently called for reform for several years, citing fairness but additionally arguing for a system that better incentivises and rewards economic growth (Cormann, 2018; Weight, 2013).[19] Western Australia occupies a powerful political position given the contribution of its mining sector to national income, and the threat that its secession therefore represents to the Commonwealth Government. As such, legislation was passed in 2018 stipulating that instead of lifting the fiscal capacity of the fiscally weaker states to that of the fiscally strongest state (Western Australia), it would be lifted to that of the stronger of either New South Wales or Victoria (the next- fiscally strongest states), reducing the degree of redistribution of the GST. Additionally, a 'floor' was introduced to ensure that, irrespective of its fiscal capacity, no state would receive less than 70% of an equal-per-capita distribution in 2022-23 and 2023-24, rising to 75% in 2024-25 and beyond (Treasury Laws Amendment (Making Sure Every State and Territory Gets Their Fair Share of GST) Act 2018, 2018). To prevent disagreement from other states, a guarantee

[19] Notably, the way Western Australia achieved their desired reforms was through calling for an inquiry by the Productivity Commission into the impact of GST distribution arrangements on national productivity and growth.

was added that no state would be worse off due to this reform, funded through a Commonwealth Government top-up to the overall GST pool. These reforms changed the fiscal equalisation standard from 'full equalisation' to 'reasonable equalisation' (Treasury Laws Amendment (Making Sure Every State and Territory Gets Their Fair Share of GST) Bill 2018 – Parliament of Australia, 2018).

The transition to the new arrangements has resulted in Western Australia receiving a steadily-increasing share of GST funding, meaning its total assessed fiscal capacity now exceeds that of other states (Commonwealth Grants Commission, 2024). Nonetheless, GST distribution remains strongly redistributive towards fiscally weaker states.[20] Additionally, though the total GST pool shrank following the 2008 global financial crisis and has not recovered to pre-2008 levels since, the size of the pool has remained relatively stable since the early 2010s, and has even increased somewhat in recent years (Commonwealth Grants Commission, 2024; PwC, 2020). This is in part because, since 2021–22, the Federal Government has topped up the GST revenue pool. Most states have therefore seen a year-on-year increase in the amount of GST funding over recent years.

Assessment

Though Australia's system of fiscal transfers to states has been criticised for relying too much on specific purpose payments, the recent introduction of broader national agreements has been welcomed for giving states increased flexibility in how to achieve mutually agreed objectives. Compared to local and city-regional governments in England, Australian states also do receive a fairly balanced amount of 'specific purpose' and 'general purpose' funding – in recent years the two have been more or less equal in magnitude.

The Australian Federation is generally seen as a very effective example of horizontal fiscal equalisation, achieving a high degree of equalisation of fiscal capacities based on a thorough and comprehensive assessment of both differential revenue capacities *and* needs (Coppel, 2020; McGovern et al., 2002; Spahn and Shah, 1995). From the perspective of reducing geographic inequalities, therefore, the Australian framework of horizonal fiscal equalisation is a successful model. The institutional arrangements for determining the distribution of GST revenues – through the independent statutory body of the Commonwealth Grants Commission – are also recognised as robust (Coppel, 2020).

Nonetheless, there are notable tensions in the system, particularly those emanating from fiscally stronger states like Western Australia. Relatedly, despite the Commonwealth

[20] The biggest 'losers' from the transition to the new distribution arrangements so far have been New South Wales, Victoria, and Queensland.

Grants Commission's aim of preserving 'policy neutrality', the system has been criticised for weakening incentives for states to pursue economic, tax, and expenditure reforms aimed at strengthening their fiscal position (Koutsogeorgopoulou, 2007). From the perspective of regional development more specifically, the strongly redistributive system has been criticised for not allowing states that have achieved a degree of economic growth to reinvest in infrastructure safeguarding their future economic capacity (Tonts et al., 2013).

The interaction between the GST redistribution system and funding through specific purpose payments is also an important feature of the Australian system. Since the GST allocation formula considers the amount of SSP funding each state receives, any additional funding awarded to specific states, such as for infrastructure projects, tends to reduce their share of GST revenue. For example, Tasmania has been awarded funding over the next several years to support a stadium redevelopment, and as a result their GST revenue for the coming years will be adjusted downward (Interview, senior Treasury official).

> *"You will see politicians, like education ministers, tie themselves in a knot about getting 20 more dollars in another state. And you know, it amuses us no end because we know that they're probably going to lose quite a bit of that $20. Through the GST redistribution."* (Interview, senior Treasury official)

While SSPs provide a way for the Federal Government to support particular policy priorities and to invest in particular geographic areas, such investments do not therefore tend to increase the overall resources available to the relevant states, above their entitlement through the GST-based fiscal equalisation mechanism. The way that SSP payments interact with horizontal equalisation through the GST therefore in effect limits the amount of redistribution or spatial targeting of funding that is possible. The Commonwealth is in certain cases able to support investment in particular states while avoiding this being adjusted-for in GST revenue if the Treasury makes a decision that particular payments should be discounted by the Commonwealth Grants Commission in calculating a state's GST allocation. However, in practice this mainly happens when funding is deemed to be in support of nationally strategic objectives, such as infrastructure investments to support the Olympics (Interview, senior Treasury official).

So, while Australia's fiscal equalisation mechanism evens out states' ability to provide services, as shaped by their differential tax-raising capacity and the cost of service delivery, the system prevents spatially-targeted investments over and above each state's GST allocation designed to help less developed states address long-standing structural disadvantages (e.g. a historic undersupply of social housing or physical infrastructure).

> *"I mean, I agree that, all else equal, the GST redistribution system can only achieve equality so much. Again, if there are those stock issues or historical factors that we're not addressing, and the CGC [Commonwealth Grants*

Commission] doesn't address those, then it's never actually going to quite achieve equality, right? But it generally does a very good job of it." (Interview, senior Treasury official)

As responses to a recent review of Australia's horizontal fiscal equalisation framework emphasise, the fiscal equalisation framework "only compensates states for the higher costs incurred by governments in delivering its services to [..] remote communities, [..] it does not provide additional funding in excess of the cost of compensating for the disability so as to be able to reduce the disability", as the policy "is not designed to close the gap in unmet need, or address extreme disadvantage, backlogs in service provision, infrastructure deficits or economic efficiency" (Productivity Commission, 2018: 119). One might therefore characterise the Australian system as supporting relative equality of living conditions across states (through access to public education, healthcare, social security, and public services), but with less emphasis on addressing persistent underlying infrastructural and economic inequalities.

We now turn to funding for local government (section **Error! Reference source not found.**) and other sub-state areas (section 0).

Funding for local government

The main administrative layer below the state level are local councils. Local councils as a whole raise around 65% of their revenue themselves, in the form of:

- Council rates (around 37% of total revenue)
- Fees, charges, and sales of goods and services (around 26% of total revenue)
- Interest income (around 2% of total revenue)

The limitation of local governments' tax raising powers to a single tax – property rates – in addition to various fees and charges, is imposed by the Federal Government. Additionally, all Australian states place restrictions on the ability of local governments to raise revenue. Notably, most states operate controls on allowed increases in council rates, through rate-pegging or rate-capping (Sansom, 2020).

Like in England, the responsibilities of local governments in Australia have grown considerably over time. From initially only concerned with providing basic infrastructure like street lighting and waste collection services, in the postwar era their functions have expanded to a more diverse range of activities, such as youth services, libraries and recreation centres, community health, environmental management and local economic development. This has been in part a response to rising expectations of the public, and in part the result of the devolution of service-delivery functions from higher levels of government (Brackertz, 2013; Lawrie and Ryan, 2024). In addition, increased regulatory requirements from higher levels of government in areas such as asset management, land use planning and community planning, place additional pressures on local governments (Lawrie and Ryan, 2024).

To provide these services and comply with these requirements in a context of restricted own-revenue raising capacity, local governments rely on a substantial amount of funding from higher levels of government. Local governments receive just under 20% of their total revenue through intergovernmental transfers.[21] The majority of these are revenue grants and subsidies, and around a third are capital grants (Australian Bureau of Statistics, 2024a). Intergovernmental transfers come partly from the Federal Government, and partly from the states. The main source of federal funding for local government are financial assistance grants paid to the states who in turn distribute the funding to individual local governing bodies (DITRDCA, 2024a).

Financial Assistance Grants to local government

Since the Federal Government is constitutionally prohibited from interfering in state matters (and local government comes under state jurisdiction)[22], the Federal Government provides funding for financial assistance grants to the states and territories, who in turn distribute the grants to local councils. Federal Financial Assistance Grants for local government consist of two components (Australian Government, 2024b: 114):

- A general purpose component which is distributed between the states and territories on a per capita basis, and
- A local road maintenance component which is distributed between the states and territories according to fixed historical shares.

In most states, the general purpose component makes up the majority of financial assistance with the road maintenance component constituting a minority of the funding (between 25 and 44%). In Tasmania and the Northern Territories, however, the road component is larger than the general purpose component (Australian Government, 2024b: 114).

While local government financial assistance provided to states is ring-fenced and states are thus not able to use this funding for other purposes, they have control over how these grants are allocated between local authorities. Each state has a Local Government Grants Commission which determines the appropriate distribution of funding between

[21] The remainder is made up from various sources, including income from public enterprise and fines, and assistance through the Natural Disaster Relief and Recovery Arrangements (Australian Bureau of Statistics, 2024a; Australian Local Government Association, n.d.).
[22] Though in practice the Commonwealth has often found ways to exercise expenditure power in a way that bypasses the states, and thus could be argued to contravene the principle that the federal government do not encroach on state government functions (Stewart, 2023).

local councils. The Local Government (Financial Assistance) Act (1995) specifies that the allocation of general purpose payments to local government must adhere to a similar principle of horizontal equalisation as that used to govern inter-state allocation of GST funding.[23] Therefore, each state uses a broadly similar methodology to calculate funding allocations between local councils, by taking into consideration each local council's own revenue and expenditure by function, estimated resident population, land value, and the total length of local government-maintained roads (Government of South Australia, 2013; Northern Territory Government, n.d.; NSW Local Government Grants Commission, 2020).[24] States then decide to accept, or not, the distribution recommended by the Local Government Grants Commissions.

Specific purpose payments to local governments

Local governments also receive federal funding through specific programmes, such as the Roads to Recovery Program which supports the construction and maintenance of local road infrastructure (DITRDCA, 2024c) or the Changing Places Program that provides funding to build accessible toilet facilities in local government areas across Australia (DSS, 2024). There are many other examples of such specific funds. Local governments are in some cases also able to bid for funds that are also open to other levels of government and non-governmental organisations, such as the Housing Australia Future Fund (Housing Australia, 2024a). Allocation mechanisms and funding conditions vary between these programmes. Often the federal government only provides a percentage of funding for programmes with local governments, and sometimes states, expected to provide the rest. Part of specific purpose funding received by local government are grants specifically for regional development. These are described in more detail in section 0.

Assessment

Though they remain limited compared to the English context, the functions of Australian local governments have grown significantly over time, partly due to devolution of responsibilities by higher levels of government (Brackertz, 2013). Although the provision of specific purpose payments and general revenue assistance partly recognises this increased remit, the resultant increase in the revenue base of local authorities has not

[23] The principle "ensures that each local governing body in the State or Territory is able to function, by reasonable effort, at a standard not lower than the average standard of other local governing bodies in the State or Territory. It takes account of differences in the expenditure required by those local governing bodies in the performance of their functions and in the capacity of those local governing bodies to raise revenue" (Government of Australia, 1995).

[24] Small differences in exactly how these factors are calculated may exist.

been proportional to the expanded range of local government services, resulting in 'unfunded mandates' (Lawrie & Ryan, 2024). This has resulted in strains on local government funding (Australian Local Government Association, n.d.). Funding pressures are particularly an issue in rural areas, where local government often has to step in to provide essential services not provided by either the private sector or the state, such as childcare, elderly care, welfare administration, environmental management, and power, water and sewerage maintenance (Michel and Taylor, 2012).

In response to concerns over financial sustainability, local government has been subjected to extensive reform over recent decades. Aside from (forced) amalgamation of local authorities as detailed in section 0, these reforms have mainly taken the form of re-definitions of the responsibilities of local governments, amendments to reinforce the democratic oversight and obligations of elected officials, and increased prescriptions for financial and performance auditing by both external (state-level) and internal auditor (Sansom, 2020). Assessment indicates that, although the first of these reforms typically resulted in some reduction in expenditures, amalgamation has overall failed to result in the promised efficiency savings (Drew et al., 2024; Mughan, 2019). The effectiveness of the remaining reforms has not been comprehensively evaluated, but the fact that an inquiry into local government sustainability is currently ongoing (Parliament of Australia, 2024) suggests that this is still an issue of concern. The overall impression is that local authority funding and governance in Australia shares many of the same problems as are found in the English context, including insufficient resource to meet expanded responsibilities and cost pressures, limited own revenue-raising powers, a weak constitutional position, and concerns over leadership and capacity (Brackertz, 2013; Haslam McKenzie, 2024; Sansom, 2020).

Funding for other sub-state areas

Funding for economic and regional development

Both the Federal Government and state governments provide funding for regional development.

One of the major place-based policies over the last ten years has been a set of city deals, modelled on the UK policy of the same name, focused on nine cities across Australia. City deals are agreements between the Federal Government, state government, and local government, and provide frameworks for coordinating investment, planning, and infrastructure provision to support economic development over a multi-year period

(DPMC, 2019).[25] The policy was adopted as a way to address urban challenges in Australia such as the need for infrastructure and increased housing supply, through more effectively bringing together different levels of government and the private sector (AHURI, 2017). Following the nine city deals, three regional deals were additionally agreed. As well as providing a framework for bring together existing funding, these city and regional deals come with a substantial amount of new funding from both Commonwealth and state level. The table below sets out estimated total Commonwealth funding spent or committed under each city and regional deal between 2019-20 and 2025-26.[26]

Figure 2: Australian City and Regional Deals from 2019-20 to 2025-26

City/Regional Deal	Total federal funding 2019-20 to 2025-26 (in $million Australian dollars)
Adelaide City Deal	161.0
Albury Wodonga Regional Deal	78.2
Barkly Regional Deal	27.3
Darwin City Deal	99.7
Geelong City Deal	181.2
Hinkler Regional Deal	10.8
Hobart City Deal	1,019.8
Launceston City Deal	203.2
Perth City Deal	400.7
South East Queensland City Deal	363.9
Townsville City Deal	276.6
Western Sydney City Deal	2,695.6
Total	5,517.9

Source: Parliament of Australia (2022) Regional Australia measures – Budget Review 2022–23.

In addition to the above federal funding, the deals involve substantial state funding. For instance, the Queensland Government has committed $618 million to the South East

[25] Most deals are for a period of 5-7 years.
[26] This was as of the 2022-23 budget review. Some city and regional deals (e.g. the South East Queensland City Deal) extend beyond 2025-26, and in these cases the table does not provide the full amount of funding to be received.

Queensland City Deal (Queensland Government, 2023), and the Government of South Australia has committed $364 to the Adelaide City Deal (Commonwealth of Australia, 2019).

Not all large Australian urban areas have a city deal – e.g. Melbourne, Newcastle, and Wollogong are sizable cities without one – and only three regional deals have been agreed leaving most of regional Australia without such a deal. The deals, unlike in the UK context, have involved no discourse or promise of devolution, possibly because in Australia states already have responsibility for planning and major infrastructure and service delivery. On the contrary, the city deals have been characterised as a way for the Federal Government to insert itself into state governance and make nationally-strategic infrastructure investments (Pill and Gurran, 2023). This, for some, has come at the expense of developing whole-place strategies (Spiller, 2022).

The current Government has honoured commitments made in existing deals but has not announced further deals.

Other federally-funded regional development and place-based funding programmes over the last ten years include:

- The Growing Regions Program (2023-2028), which provides funding to local governments and not-for-profit organisations on a competitive basis for capital projects designed to improve liveability, social cohesion, and local amenities in rural and regional Australia, up to a total of $600 million over four years[27] (DITRDCA, 2024b).
- The Regional Growth Fund (2018-2022), which provided grants of $10 million or more (to a total of $272 million) for major transformational projects to support long-term economic growth and job creation in regional Australia (DITRDCA, 2019).
- Regional Jobs and Investment Packages (2017-2020), which provided a total of $222 million in federal match-funding for projects in ten regions to help them diversify their economies, stimulate long-term economic growth and deliver sustainable employment (DIIS, 2017).
- The Stronger Communities Programme (2015-2024), which provides grants of up to $20,000 (to a total of $181 million over eight rounds) to local governments and community organisations for small capital projects delivering social benefits for local communities (DIIS, 2024; DITRDCA, n.d.).

[27] The Growing Regions Fund takes the place of precursors like the Building Better Regions Fund (until 2022) and National Stronger Regions Fund (until 2016).

Most of these funds are or were allocated on a competitive basis, though in the Stronger Communities Programme projects were selected and put forward by the local member of parliament (DIIS, 2024).

The Federal Government has also recently created the Housing Australia Future Fund, which will provide $10 billion in co-investment finance to deliver social and affordable housing. Community housing providers, as well as states and territories, local governing bodies, and local, state or territory government-owned corporations, can apply on a competitive basis for availability payments[28] or concessional loans to build or renovate social and affordable housing (Housing Australia, 2024b).

States and territories provide their own funding for place-based programmes. Policy priorities and funding arrangements vary strongly across states, making it difficult to provide an overall summary. Below, funding mechanisms in Western Australia are described as a generally positively-regarded example of how to fund regional development activities.

Regional development funding in Western Australia

Western Australia is arguably the state that has invested most strongly in regional development over past decades, in part enabled by the substantial revenue raised through mining royalties. The Western Australian Government passed legislation in 2009 stipulating that each year, 25% of these royalties, up to $1bn, are to be paid into a fund reserved for the provision of infrastructure and services, economic development, and the creation of jobs in regional Western Australia (Government of Western Australia, 2009). As a result of this 'Royalties for Regions' programme, resources available for regional economic development in the state are considerable, compared to past state spending on regional development and compared to other states (van Staden & Haslam McKenzie, 2019), especially considering the small population of regional Western Australia (just over 600,000 in 2023). As a senior state civil servant put it:

> *"Well, there's more money in the system. You know, money's always competitive. I mean, what I'm what I'm talking about, though is really economic development. You know, I'm not talking about kind of putting, you know, an extra teacher in the classroom. [..] I'm talking about it from an economic development side, and that picks up on the social side of development as well. [..] No, I think we've been, we've been quite fortunate, fortunate. If you drive around WA, you know, we have good roads [..], we have dialysis machines for Aboriginal communities in the north because of diabetes, you know, I do think we do pretty well in terms of the*

[28] Availability payments are a type of payment sometimes used for public private partnership (PPP) projects, in which a public agency makes fee payments to a contractor upon completion of the agreed project.

> *infrastructure support, you know, compared to other places."* Senior civil servant, Western Australian Government

This same participant informed us that the state Government has in fact struggled in the past to allocate the full amount of regional development funding available.

Though the Royalties for Regions programme is certainly not free of criticism (de Garis et al., 2017)[29], it has several noteworthy positive features. The programme is entrenched in legislation, ensuring its longevity. This has enabled regional development strategies to focus on improving the long-term economic viability and social sustainability of regional communities (van Staden and Haslam McKenzie, 2019), and, in more recent years, on enhancing the economic diversity of regional areas through supporting the growth of industries like tourism, agriculture, aquaculture, and viticulture (Buckley, n.d.). Local decision-making is additionally ingrained through the programme being administered through nine regional development commissions based across the state (van Staden & Haslam McKenzie, 2019). Chairpersons from each of the nine regional development commissions form a regional development council which reports directly to the state Minister for Regional Development, which allows the commissions to advocate for local projects directly and "makes them quite powerful" (Interview, senior civil servant in Western Australian Government). Though some state programmes are designed in a more top-down manner with funding allocated through competitive bidding, a substantial number of projects and priorities are identified through this collaborative multilevel process.

> *"Yeah, it's not all determined by [the state government]. We'll chuck some money at it and we'll give grants through a competitive process, we do have a bit of that. But there will be other things that will come through based on what's the better, you know, their individual merits. And to a large extent, I think that kind of works, you know."* Senior civil servant, Western Australian Government

On the other hand, an audit report by the Office of the Auditor General for Western Australia in 2014 found that the intended outcomes and benefits of projects funded under the Royalties for Regions program were often unclear. The report expressed concern that funding was based more on delivering physical products than on achieving meaningful outcomes for regional communities. Project evaluations similarly only reported what was delivered, rather than whether desired outcomes were met (Office of the Auditor General, 2014). It is unclear to what extent these concerns have been addressed since.

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[29] In addition, Western Australia's broader economic and industrial policy has been criticised for its over-reliance on extractive industries which are felt to have delivered disproportionate benefits to shareholders and too little to the communities that own the resources (Parker & Cox, 2020).

Structural adjustment programmes

Australia has a long history of using structural adjustment programmes to respond to economic shocks in particular industries, especially where this involves substantial and geographically concentrated job losses, as well as to support other strategic economic or environmental aims (Beer, 2015). Structural adjustment support has been provided to a range of industries in the agricultural sector, manufacturing, as well as services. Funding provided through adjustment programmes is often awarded to ad hoc bodies or partnerships set up specifically for that purpose, rather than being awarded to state or local governments. The scale and diversity of structural adjustment programmes is too great to provide a comprehensive summary here, so two notable examples are discussed below.

A well-known example of structural adjustment support in the last ten years is a package of support for the automotive industry during and after the withdrawal of Australia's remaining car manufacturers from 2013 to 2017. This included $155 million worth of federal support for affected workers and businesses in the supply chain.[30] In addition, there were two place-based funding programmes, the Innovation and Investment Funds for Geelong and Melbourne North ($24.5 million each), to support new job creation and economic growth in affected regions (DIIS, 2020; Parliament of Australia, 2014). These two funds were open to bids from any firms in the two areas that proposed to create additional jobs. The funding was jointly provided by the federal Government, the Victorian Government, and the two main (exiting) employers Ford and Alcoa, and was administered by a regional committee which included firms, unions and community agencies. Actual funding allocations, however, were decided centrally by the federal Government (Tierney et al., 2024). In part supported by this place-based investment, new employment was created in the public sector, construction, and in technical, administrative, and professional services (ibid.). However, the employment assistance programmes for displaced workers did not join up with these place-based economic development efforts by specifically re-skilling workers for these expanding industries or matching displaced workers directly with the new jobs created through the Innovation and Investment Fund (Tierney et al., 2024), instead aiming to get workers into any job (Beer et al., 2024). This limited the ability of affected workers to find high quality new employment in the local area (ibid.).

[30] The $155 million Growth Fund announced in 2014 included the $35.8 million Next Generation Manufacturing Investment Programme, the $29.8 million Regional Infrastructure Programme, the $20.0 million Automotive Diversification Programme, and the Industry Structural Adjustment Programme (Parliament of Australia, 2014). Prior to this, automotive firms received support through the Automotive Transformation Scheme, worth $3.4 billion, to generate R&D and investment to move into new areas of vehicle production. Part of the new funding announced from 2014 onwards was reallocated from these older programmes.

A different multilevel governance arrangement was used in the closure of a large coal-fired power station in the Latrobe Valley in Victoria. Hazelwood was one of the most polluting power stations in Australia. During the years of the Gillard Labor Government, it was slated for closure as a part of the Clean Energy Future policy, which also set up a $200 million fund for structural adjustment in affected regions (DCCEE, 2012; Weller, 2017, 2019).[31] However, in large part due to intervention by the then conservative Victorian Government, these policies did not succeed in closing down Hazelwood, and the structural adjustment funds were not released. Instead, Hazelwood's closure was brough about by the Victorian State Government after a fire in Hazelwood's open cut coal mine which caused significant local health concerns. The negligence of the transnational firm operating the mine (Engie) had caused fire, and the state responded with onerous new safety requirements (Interview, academic). When the closure was announced, a local committee managing the closure process instituted an innovative 'Worker Transfer Scheme' wherein younger workers from Hazelwood were offered jobs at other power stations (Snell, 2018). The State Government established a Latrobe Valley Authority, an agency reporting directly to the State Premier, to implement an extensive suite of regional development programmes. However, this arrangement effectively excluded both local government and the conservative Federal Government, which at the time was not pursuing energy transition (Weller, 2019).

The geographic scale of the interventions was also contested, with the state defining a new territorial entity, the Greater Latrobe Valley, for the allocation of structural adjustment and transition funding, which matched on to neither existing administrative geographies (like local councils or the existing RDA committees in the region) or existing 'imagined' or functional geographies (Weller, 2019). Importantly, the newly constructed territory encompassed a much larger geographical area than the (more disadvantaged) industrial communities of Latrobe City surrounding the coal power station (Holm and Eklund, 2020), and allowed the real and immediate fears and tensions over the power station closure that existed in these local communities to be de-centred in a broader debate about the future of a much wider region (Weller, 2019). As a result, projects funded through the available structural adjustment and other regional development funding mostly supported general residential infrastructure or subsidised local medium-sized businesses in other parts of the Greater Latrobe Valley, rather than directly addressing the loss of a key local industry in Latrobe City, an already disadvantaged area (Weller, 2017).

[31] Although it appears that the majority of this funding was never allocated but instead returned to the federal budget in2013 (The Hon Wayne Swan MP, 2013).

Assessment

Australia has a reasonably well-defined regional development policy, which is largely targeted at addressing what is considered to be the main axis of geographic inequality in the country: the divide between large metropolitan areas and 'the regions'. Funding for regional development is provided by both the Federal Government and the states, with the latter usually playing a somewhat bigger role in this policy area. In one notable example, Western Australia has since 2008 invested $1bn per year in its rural and regional communities through the Royalties for Regions programme – a very substantial investment given the relatively small population involved. The programme appears to have fallen in some of the same traps as local and regional development policies in England, in terms of focusing more on delivering physical infrastructure and other intermediary outcomes rather than being driven by and evaluated on actual improvements in living conditions in regional communities (Fiorentino et al., 2023; Office of the Auditor General, 2014). But the long-term commitment of the programme, and the integration of regional stakeholders into the decision-making process through regional commissions reporting directly to the relevant state minister, are positive features.

Along with explicitly regional policy, structural adjustment policies have also had an impact on local and regional outcomes in parts of Australia affected by industrial decline. This policy area has been led more strongly by the Federal Government, but often in collaboration with state and local governments. However, the two examples reviewed above evidence a lack of join-up between the federal and state level. This is not a unique feature of structural adjustment policy per se but appears to be an example of a wider issue of lack of coordination and sometimes competing priorities between the Commonwealth and the states (Koutsogeorgopoulou and Tuske, 2015; Pugalis and Tan, 2016).

The creation of bespoke ad hoc geographies for the delivery of interventions and allocation of resources within structural adjustment programmes ostensibly provides an opportunity for spatial targeting at the most appropriate scale, but in practice it has also enabled politically-driven re-scaling away from the areas that arguably are most in need of investment (Tierney et al., 2024; Weller, 2017). At the same time, local community representatives have at times been sidelined in the governance of structural adjustment programmes, raising the important question of 'who gets to have a say' over policies and funding affecting local areas.

Overall assessment and relevance for improving funding allocations to reduce geographical inequalities in England

Australian states combine a high degree of control over and responsibility for service delivery with fairly limited state tax raising powers, resulting in the necessity of substantial fiscal transfers from the federal to the state level. While this is seen by some as undesirable since it results in vertical fiscal imbalance, arguably resulting in less direct accountability and potentially creating misaligned incentives (Coppel, 2020; Koutsogeorgopoulou, 2007; Nicholas, 2003), on the other hand these transfers enable a substantial degree of horizontal equalisation (through redistribution between states). In other words, in the Australian case, the desire for vertical fiscal balance and greater accountability at the state level has over recent decades been subservient to the (perceived) need to maintain horizontal fiscal equity. The operation of a well-enshrined horizontal equalisation principle enables states to provide relatively even levels of service provision regardless of their own underlying economic and fiscal strength (Productivity Commission, 2018). Moreover, since horizonal equalisation operates, in large part, through the allocation of general purpose funding to states, they retain a fairly high degree of fiscal freedom (at least on the expenditure side) compared to sub-national governments in England.

The Australian case therefore suggests that horizontal fiscal equalisation through non-tied, non-ringfenced funding is a way to achieve a degree of sub-national fiscal freedom and policy autonomy while nonetheless ensuring (near) equal fiscal capacity.

In England, the ability of local authorities to provide adequate services for local populations and invest in infrastructure to support growth has been curtailed by sustained reductions in central government grants from 2010 onwards, alongside new un(der)funded mandates. In Australia, in contrast, the magnitude of vertical fiscal transfers from the Federal Government to states has remained fairly stable over the last several decades (from an already substantial base). This has been coupled with a continuous commitment to fiscal equalisation, in a way that has not been the case in the UK where the equalisation principle in local authority funding has been weakened through the introduction of locally-retained business rates and an increased reliance on competitive bid-based funding (Muldoon-Smith and Sandford, 2023; Phillips et al., 2019). These differences may in part be explained by the fact that in Australia an independent body – the Commonwealth Grants Commission – rather than a government department is responsible for fiscal equalisation.[32] In the UK, the Special Interest Group for Municipal

[32] Even if the operation of the Australian fiscal equalisation principle in practice is a complex and therefore somewhat opaque affair.

Authorities has called for allocations of local government funding to be similarly managed by an independent body (SIGOMA, 2024).

The Australian case represents a positive example of funding allocations for sub-national territories being handled by an independent statutory body, ensuring allocations are in line with enshrined equalisation principles rather than subject to political shifts and ad hoc funding decisions.

An additional factor may be the politically and constitutionally more powerful status of Australian states compared to sub-national governments in the UK.[33] Australian states, having been independent and more-or-less self-governing entities less than 150 years ago, are able to mount at least a theoretical threat of secession (Brenton, 2020). Moreover, the states are represented in Australia's second chamber, the Senate, giving each state an equal ability to represent its interests in national decision-making (Swenden, 2010).[34] [35] There are tensions within this system, with some fiscally stronger states (especially Western Australia) having over recent years pushed for reform leading to modification, and increased complexity, of the fiscal equalisation formula. However, the long-standing and entrenched nature of horizontal equalisation within the Australian Federation (Dougherty and Forman, 2021) has arguably contributed to the relative absence of strong grievances fuelled by spatial disparities, and a relatively subdued debate about geographic divides compared to in the UK and other countries (Weller, 2021). In this regard, the Australian system can be seen as a relatively more successful model for reducing geographic inequalities.

The Australian case therefore leads us to ask whether the long-term sustainability and sufficiency of sub-national funding (contributing to geographic equality) requires greater representation of sub-national stakeholders in national governance.

The recently established Council of the Nations and Regions could provide a first step towards this in the UK.

While horizontal fiscal equalisation through the GST produces a (nearly) equal fiscal capacity across states (Productivity Commission, 2018), there are limits to how much this mechanism alone can ensure true geographic equality. The equalisation principle centres on the capacity for equal levels of service delivery and provision and maintenance of essential infrastructure such as local roads. The capacity of this mechanism to address underlying regional strengths and weaknesses, for instance those

[33] Even if they are in a weaker position than states in other federations, such as Canada (Béland and Lecours, 2018).

[34] Though it is worth noting that debates in the Senate often follow party-political lines rather than territorial priorities. This is in part because most Australian political parties are represented at both the federal level and at the state level which means party-politics carry over from the federal to the state level (Béland and Lecours, 2018).

[35] The proposals for a new Council of the Nations and Regions in the UK may be a step in this direction.

related to historical 'stocks' of housing, infrastructure, or other assets, or to spatial (dis)advantages which have an impact on economic and demographic growth, is more limited.

Because, to an important extent, GST and other funding is allocated 'with the grain' of existing population distribution patterns, it is unable to fundamentally challenge the depopulation of certain areas, due to economic decline or other reasons.

> *"I mean do you put more funding into a place that's going backwards, you know, 'cause, it's losing population and losing economic capacity. Or do you put more funding into a place that's growing fast? Those are the sort of discussions that I haven't seen. You know, I haven't heard those discussions very often in an Australian policy context, you know. Because by default, a lot of the infrastructure and services funding is [..] going to the places that have got, you know, reasonable population growth. So, what we don't have is any sort of systematic approach to dealing with the places that are, that are really struggling."* (Interview, regional economist)

An academic we spoke to remembers that in fact there was policy discussion of this question in the past, which resulted in the conclusion that attempting to remedy population decline would be tantamount to "throwing good money after bad" (Interview, academic).[36] The non-remedial nature of GST allocations could therefore be argued to be deliberate.

Similarly, if a state pursues economic development through policies that have the effect of strengthening its tax base, this will often have the effect of reducing its GST allocation and therefore reducing the federal funding received by that state in line with the increase in own-source revenue (though the extent to which this fact actually affects decisions around economic development-oriented policies is subject to debate (Productivity Commission, 2018).

The Australian model of horizontal fiscal equalisation, while ensuring a relatively equal level of public service provision across states and thereby contributing to relatively equal living standards, arguably has a more limited capacity to address deeper-seated economic and demographic inequalities.

A further criticism of current fiscal relations between the Australian Government and the states is the increased share of total funding to states that comes in the form of specific purpose payments tied to the delivery of statutory services or national policy objectives, as opposed to general purpose revenue that can be spent flexibly on local priorities. The higher proportion of specific purpose payments or 'tied grants' (relative to the past) limits the ability of states to allocate funds in line with their own policy choices, and

[36] It is also often argued that population decline – at least to the extent that this results from household relocation decisions – should not be resisted but in fact encouraged since it contributes to the efficient allocation of human capital to the most productive places.

commentators have argued there is further scope to reduce federal conditional grants to strengthen their fiscal autonomy (Koutsogeorgopoulou, 2007; Koutsogeorgopoulou and Tuske, 2015).[37]

Nonetheless, Australia's state-federal fiscal framework still arguably provides a fairly even balance between accountability to the Federal Government (through specific purpose funding tied to National Partnership Agreements), and flexibility for states to allocate funding according to their own priorities (through general purpose funding). This balance ensures that states and territories are held accountable for using Commonwealth funds effectively and for contributing to national goals, while allowing them the independence to address local challenges in ways that make sense for their specific contexts.[38] In the English context, the balance between central oversight and local autonomy skews more strongly towards the former, given the more centralised nature of the UK governance system. Though in some areas, devolution agreements have granted combined authorities more flexibility in spending decisions, for example through 30-year investment funds, funding to English local authorities currently is almost entirely made up of specific purpose grants, with general purpose funding (the revenue support grant) amounting to less than 2% of total grant revenue in 2022/3 (MHCLG, 2024).[39] In addition, cuts to local government grants mean English councils have needed to spend an increasing proportion of their own-generated revenue on statutory services, resulting in even less local spending discretion (Phillips et al., 2019).[40]

Comparison with the Australian case raises the question whether local authority funding in England now skews too heavily towards specific-purpose grants and there is a need for a greater proportion of general-purpose funding to restore balance.[41]

While Australia has relatively strong and well-developed processes to promote fiscal equality between states, the mechanisms in place to support within-state equality are perhaps somewhat less robust, and certainly less clear and transparent. This is in part due to its federal constitution, with states having substantial autonomy over how much they prioritise spatial equality and how they attempt to achieve it, with neither the Federal

[37] E.g. Article 9 of the European Charter of Local Self-Government states that "As far as possible, grants to local authorities shall not be earmarked for the financing of specific projects. The provision of grants shall not remove the basic freedom of local policy discretion within their own jurisdiction." (Council of Europe, 1988).
[38] Although in certain policy areas the Australian multi-level governance system suffers from blurred responsibilities, problematising accountability to the public (Koutsogeorgopoulou and Tuske, 2015).
[39] This is to a large extent the result of the introduction of the Dedicated Schools Grant in 2006, as opposed to schools being funded as part of the broader Revenue Support Grant and other council income as was previously the case.
[40] According to Local Government Financial Statistics, 62% of total service expenditure was dedicated to education and social care in 2022/3 (MHCLG, 2024).
[41] It may be argued that English local authorities are not equivalent to Australian states, but the former nonetheless hold substantial statutory responsibilities as well as bearing non-statutory responsibility for local economic and social development, business support, community cohesion, public health, culture and recreation, and a range of other functions central to the aim of reducing geographic inequalities.

Government nor local authorities having much power to shape these decisions. There have been criticisms that state governments often divert more revenue to metropolitan areas than to 'the regions' (Berry, 2011; Tonts et al., 2013). The Federal Government has, over recent decades, attempted to influence within-state geographic outcomes through regional development policy (i.e. policies primarily directed at 'rural and regional' Australia). However, due to various reasons, the ability of the Federal Government to substantially shape regional development has remained fairly limited, and the states remain the primary actors in this policy area (Haslam McKenzie, 2024; Weller, 2017).

States vary in their approach to regional policy and the amount of funding dedicated to this aim. Western Australia's Royalties for Regions programme is a notable example of a well-resourced regional development policy. While the programme has been critiqued for a lack of an outcomes-based approach to funding decisions and evaluation (Office of the Auditor General, 2014), its emphasis on improving the local capacity and sustainability of regional communities is commendable. This long-term focus has been aided by enshrining the commitment to reinvesting 25% of mining royalties into regional communities in legislation (Buckley, n.d.), while local engagement is facilitated through involvement of regional development commissions and local governments in decision-making processes (Office of the Auditor General, 2014; van Staden and Haslam McKenzie, 2019).

Australian regional policy examples highlight the importance of coordination in a multi-level governance system, longevity of funding commitments to regional development, right-sized geographies for intervention and spatial targeting, and ensuring involvement of local and regional stakeholders in decisions about funding and how this is used.

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