Federalism and Economic Stimulus in Canada, USA and Australia: Cooperation and Competition in Responses to the Global Financial Crisis

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Introduction
Federal systems exist to divide power and to promote diversity but face circumstances that require policy outcomes coordinated across jurisdictions. This paper compares three relatively similar federal countries with a similar coordination challenge regarding macroeconomic and fiscal policy. Historically, meeting coordination challenges such as building the welfare state or updating economic integration, have been defining features of the federal experience of the United States, Canada and Australia. Since the late 1980s, however, federal theory and practice has also stressed decentralization, subnational autonomy and market-preserving values (Ostrom, 1987; see review in Hueglin and Fenna, 2006: 319-22). This paper, part of a longer term project on multilevel policy coordination in federal systems, addresses the question of whether federal systems, despite their decentralization, can still deliver sufficient coordination when politics and policy demand it. It examines an important and dramatic case: the responses to the Global Financial Crisis, the global recession and their aftermath. These events present a compelling test of the effectiveness of federal coordination although, perhaps surprisingly, not the toughest case.

Federal theory would suggest two general propositions about how federal systems of government deal with coordination problems. The first proposition is that the more integrative the federal system, the more readily it will achieve effective policy coordination. In this context, integrative refers to systemic capacity for achieving federation-wide decision-making, which in turn is affected by relative social and political cohesion, by constitutional design including legislative, executive and judicial institutions, and by the style and history of intergovernmental relations. Literature on the three federal systems leads one to predict that Australia is the most integrative, followed by the United States, and Canada being the least.¹

The second proposition arising from federal theory is that policy coordination can be achieved through competitive as much as through cooperative or collusive processes. National decision-making need not be required in every circumstance, and the self-organization of the market or of decentralized competition can lead to effective outcomes. The literature on competitive federalism in the three federal systems² is much less developed, but given that these ideas find much of their inspiration in US practice, one can hypothesize that the USA would be the leader in this respect. In particular, one can examine whether competitive federalism is a sufficiently effective substitute in the absence of national policy coordination.

Policy coordination itself is an elastic term, and varies significantly by the characteristics of a policy area, and the contextual circumstances of the potential set of problems and solutions. This paper is part of a larger project which explores the logic and history of how policy problems

¹ Federation-wide coordination implies all governments and the entire federation territory; such efforts are often termed “national”, although that can be a problematic and contested term in Canada. For recent literature on federal integration and coordination see Watts, 1999; Baier, 2006; Hueglin and Fenna, 2005; Fenna, 2007; Watts2008 and Bakvis and Brown, 2010.

² There is no comparative study of competitive federalism as such. For works that cover one or two federations see Fletcher, 1991; Kincaid and Kenyon, 1991; Vogel, 1995; Painter, 1998; Brown, 2002. There is also the political economy school, see for example Tiebout, 1965; Breton, 1987; Buchanan 1995.
have been defined and resolved in multilevel contexts. In each of three policy cases, I seek a set of benchmarks or parameters by which one can judge if effective policy coordination is taking place. The same parameters are applied to the three federations, but differ according to the policy case.

While ideally a study of policy coordination might involve an examination of all the world’s federal systems, as well as some non-federal systems, the project is confined for now to the three systems as a “most similar” comparative set. The small set of comparison allows a much richer narrative on policy histories and intergovernmental dynamics that could not be captured in a broader study. Canada and the United States share a continental history, economy and somewhat similar social development. Canada and Australia are both parliamentary federations uniting a small number of constituent units; and both are middle powers. On the other hand, Australia’s federal constitution is heavily modeled on the USA, in its distribution of powers, its elected upper house, and its system of judicial review. In any case the three systems have enough differences in their institutional design and political development to illustrate a rich and suggestive array of the varieties of federal coordinative experience.

**Economic Stimulus as a Policy Coordination Issue**

The Global Financial Crisis (GFC), the associated near-global recession in 2008-09, and the continuing issues of financial stability, sustainability and fiscal consolidation represent a dramatic package of policy challenges. The key policy fields affected are macroeconomic and regulatory (as mainly affecting the financial services sector). For all states involved, the GFC has been an issue of international financial governance and, at least to some degree, macroeconomic coordination and cooperation. It is a multilevel challenge involving national governments, international organizations and major private actors. This involved, among other policy issues, determining appropriate macroeconomic management of national economies once the GFC began to affect output and employment, such as reducing interest rates, provision of quantitative easing, lowering taxes, stimulus spending, and providing loans, subsidies or equity infusion for specific failing firms. It entailed, as well, policy to revise, often dramatically, the overall budgetary stance (deficit/surplus, debt levels) of governments. In the medium to longer term, the task turns to coordinating efforts of fiscal consolidation, i.e. returning to sustained budgets and debt burdens. It has also involved immediate regulatory action to shore up liquidity and stability of national financial sectors at risk of individual and institutional system-wide failure, and over the medium term, regulatory reform of those systems.

For federal systems the multilevel aspect is complicated by the shared jurisdiction of many of the macroeconomic policy levers at play as well as the regulatory authority. In addition, for geographically large and diverse federations—such as the three compared in this paper—the effects of the global recession and the appropriateness of policy responses is further complicated by regional economies within the federal economic union, with potentially different exposures to global events and differing abilities to withstand external economic shock.
Furthermore, four features of federal practice provide especially pertinent context for how federal systems deal with economic crisis: 1) the economic and monetary union; 2) tax and expenditure allocation; 3) intergovernmental transfers; and 4) coordination mechanisms.

All federations (and many federal-type systems, notably the European Union) have an economic and monetary union at the heart of their constitutional and political arrangements. Economic unions serve to capture economic benefits such as market integration, increased bargaining power, the sharing of costs, and the pooling and sharing of risks (ECC, 1991:31-3; for discussion see Brown, 2002: 51-58). A common currency and common monetary policy are usually seen as key to a mature, deeply integrated union. Monetary policy competence is almost always a federal (or, if one prefers, central) government role. Most federal systems also involve a more or less independent central bank which may include regional governance features. Nonetheless, the monetary side of macro policy is firmly in central hands, even if sometimes challenged politically by the constituent unit governments (Boadway and Shah, 2009). Monetary policy must often work effectively with financial sector regulatory authority and many federal systems divide or share regulatory responsibility between the central and subnational governments. Federal authority typically extends to nationally incorporated banks, insurance, securities and related sectors (implying national and international scope of operation), whereas subnational governments authority is more often over more regionally-scooped institutions, such as banks, trusts, credit unions and other firms operating on a province or state-wide basis only. The distinction is often blurred.

The sharing and distribution of macroeconomic authority is even more widespread with respect to fiscal policy where tax allocation and effort is typically shared, and where there is at least a degree of decentralization and autonomy in the budgetary policy of constituent unit governments including, in many federations, the capacity to borrow at home and abroad to finance debt. In many federations there are constitutional or legislated provisions on the exercise of fiscal policy autonomy by subnational governments (balanced-budget provisions, referenda for new taxes, federal prohibitions or control of foreign borrowing, etc.). Federal constitutions and longstanding political practice determine the structure of taxation and spending responsibilities but the actual application of fiscal power depends on diverse conditions across subnational governments, involving regional economies, social need, and political culture and ideology across constituent units.

Vertical and horizontal fiscal gaps occur both naturally and by design in federal systems as the constituent units never have identical fiscal capacity, let alone identical expenditure needs. Federations provide intergovernmental transfers in the form of shared tax proceeds, conditional and unconditional grants, loans and other instruments. One expects central government fiscal capacity to be sufficient to take care, not only of their own direct spending responsibilities but also to contribute through transfers to a more efficient and equitable provision of public goods and services by subnational governments. In the process these transfers promote national (federation-wide) standards in policy and programs, as well as horizontal fiscal equity, and often both. In the heyday of Keynesian macroeconomic policy dominance, central governments were also expected to have a dominant fiscal position to take the lead role in macro stabilization (Boadway and Shah, 2009: chapter 14).
One of the paradoxes of the federal form of government is that effective macroeconomic policy management is required – a stable national economy and the sustained integrity of national economic integration are key objectives of virtually any federal union – but can be very difficult to achieve due to the very element of federalism. The requirement of diversity within unity and the provision for autonomous subnational governments with at least a minimum capacity for fiscal policy (if not some aspects of monetary policy) presents an ongoing coordination challenge. Indeed, a single macro stance may not be desirable given differing economic endowments and structure of regional economies, but usually a single policy stance is unavoidable or otherwise has overwhelming merit (e.g. single exchange rate). Nonetheless there is going to be political controversy about where the balance of policy should lie in a multi-region union. National counter-cyclical fiscal policy can be especially difficult to achieve where fiscal decentralization is sufficient that the budget position of subnational governments can potentially neutralize the central government’s macro stance. And there is often controversy within a federal system about particular macroeconomic objectives, reflecting ideological as well as regional diversity.

Nonetheless, federal systems do attempt macroeconomic and financial sector coordination, by a variety of means. Some means are formal, such as national legislative schemes which are imposed upon subnational governments, and includes national budget statements backed up with legislative measures where required. Specific intergovernmental agreements can also draw parameters around collective governmental action. Other federal processes such as debate and review in upper houses and in intergovernmental ministerial councils provide formal structure to consensus building and federation-wide decision-making. More informally, often working alongside the formal processes, are party organizations and networks, professional organizations and their norms and, crucially with respect to almost all aspects of macroeconomic policy, the existence of broad market discipline whereby global, national and even local financial markets readily communicate norms and expectations for policy outcomes.

Apart from the means of coordination, can one more specific about the ends – i.e. what does effective policy coordination look like? To summarize some of the points raised to this point with respect to the coordination challenge in the GFC and recession in the period of 2008-13 (and for simplification in this paper leaving out issues of financial sector regulation), I propose the following benchmarks:

1. The collective provision of sufficient economic stimulus to stabilize the national economy, relevant to the severity of the external shock and the impact and depth of recession.\(^3\)
2. Synchronicity of overall national macroeconomic efforts between the central and subnational governments, and among the subnational governments.
3. Flexible adjustment as required to intergovernmental fiscal arrangements.

\(^3\) I set aside for now the issue of whether the provision of economic stimulus, i.e. a Keynesian response to crisis and recession, is the correct or desirable policy response, but rather concentrate on the systemic capacity to deliver such a response.
Overview of Key Developments in Three Federations, 2008-13

United States
As John Kincaid has written, the fact that the USA was the epicenter of the causes of the GFC, one of the economies most dramatically affected by the crisis and the concurrent recession, and that its federal government was the epicenter of the global response to the crisis, tends to obscure the domestic governance challenges for the federal system as such (Kincaid, 2010). American economic growth, including employment and investment, consumer spending and confidence, and returns in the stock market, began to slow in late 2006 as the slowly accumulating crisis of the housing market and the associated mortgage debt emerged. The contagion effect on the global economy, led by countries with globally integrated banks and other financial institutions, but also affecting any economy dependent on global demand, went into high gear after the collapse of Lehman Brothers in September 2008. The United States economy officially entered recession in December 2007, not to emerge until June 2009, losing 4.1 percent of its GDP. A weak recovery continued into 2010 then faltered, although a “double dip” recession did not take place. In 2014 growth is now projected to be 2.2 percent of GDP. At the peak of the recession, US unemployment officially exceeded 10 percent, which understates real unemployment.

The federal government’s response to the crisis can be broken into three phases. The first is the set of responses taken by the Bush Administration and by Congress throughout 2008 to stimulate the economy through tax cuts and spending, to provide relief to financial institutions burdened with near worthless debt assets, and to guarantee some domestic mortgages. The second, and more comprehensive, is the set of measures undertaken by the Obama administration (with Democratic majority in both houses of Congress until January 2009, and in the Senate afterwards). The most ambitious of these was the omnibus American Recovery and Reinvestment Act (ARRA) of February 2009 – an $830 billion collection of tax relief measures, infrastructure projects, and the expansion of federal social program spending to the States (mainly health and education). In addition, the Obama administration negotiated loans to major firms in the automobile sector, provided further tax credits for home buyers, and, with Congress, achieved an initial overhaul of the financial regulatory system. While outside the direct control of the US Government, the Federal Reserve undertook its major program of quantitative easing. The third phase, in some respects continuing, has been the extension or continuation of a variety of tax and expenditure measures, as well as monetary policy, aimed at sustaining recovery.

Throughout all three phases the issues of economic stimulus and regulatory reform have been ideological and partisan. The Bush government assumed much initial blame for the GFC in 2008, contributing to the Democratic Party’s victories in the Presidential and Congressional elections in that year. By early 2010 Republican forces had recovered as large parts of US public opinion recoiled at the increased federal deficit and debt and the perception of “big government”

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4 Valuation in dollars noted in this paper is according to the national currency in each case, i.e. US, Canadian or Australian dollar. In the period 2008-13 the Canadian and Australian dollars was valued between .90 and 1.10 $US, and thus for the order of magnitude analysis here, the three currencies can be considered as approximately the same.
promotion in the guise of economic recovery policy. This sentiment led to, and fed from the “Tea Party” movement of economic libertarians, who had a significant impact on Congressional midterm elections in 2010 and in State politics.

As for the States, their collective financial situation went from bad to worse as the recession approached and reached its peak. In some key states, such as California and Florida, where revenues from land transactions and sales taxes constituted the core of own-source revenues, public finances were devastated. Most state and local governments faced the prospect of sharply declined revenues but also significant increases in social services spending as unemployment grew and consumer sales fell. State pension funds, devastated by market losses, continued to be a major political and financial liability. Virtually all states, however, were under the burden of balanced budget constitutional and other provisions which effectively prevented them from running deficits. Some states were able to access “rainy day funds” (reserved surplus); some were able to increase selected own-source revenues, and most states looked to the federal government to provide immediate relief. The extent of the states’ pro-cyclical stance varied according to the depth of their revenue losses and the general state of public finance prior to the onset of the GFC. In practically all states public sector lay-offs continued through 2010 and indeed accelerated as the federal stimulus wound down (Conlon and Posner, 2010; Ter-Minassian and Fedelino, 2010; Gamkhar and Pickerell, 2012). By 2011 US state primary deficits were, on average, under .5 percent of GDP, but state debt was, on average, approaching 25 percent of GDP (Blochliger, 2013).

The State Governors, working directly with the Obama administration and with Congress, did have a major impact on the ARRA in particular, arguing that federal transfer relief for such programs as education would prevent a much worse unemployment situation. They of course did not get all they sought, although in the end more than half of all the ARRA funds flowed through state and local government hands, providing enormous fodder for both intergovernmental and intrastate debate (Gordon, 2014). The Obama administration made significant efforts to forge an effective intergovernmental partnership, which was of course essential for public capital projects in particular to have an impact on the recession.

The ideological divide in Washington over how to respond to the crisis also affected state politics and responses – as proxy fights for national politics, but also on the merits of state and local responses. Some states, led on the Republican side by South Carolina Governor Mark Sanford, refused federal aid on essentially partisan grounds. Many states found it difficult to juggle expenditure priorities distorted by federal transfers (most commonly seen in education where federal funds were conditional upon “maintenance of effort”). States also chafed at the many conditions big and small embedded in the ARRA that had little to do with economic recovery but lots to do with federal political priorities, affecting accountability, administration generally and intruding into policy domains such as climate change, education and others. Still, the Obama administration remained flexible on implementation, agreeing to state waivers to have state program provisions or standards stand for federal ones. On the whole it can be said that federal measures in response to the GFC and recession, implemented and designed in cooperation with the States, did address the key fiscal arrangements upon which the States
depend. However, as noted above, the fiscal consolidation problem remains for the States, especially their debt loads and pension liabilities. In tackling these issues over the coming years, any further help from the federal government would have to be in doubt, indeed federal transfers are surely designed for cuts, given the size of the fiscal consolidation challenge for the central government (Blochliger, 2013).

Canada

As the Canadian economy is heavily integrated globally and continentally, Canada could hardly avoid the effects of the GFC even if its main causes were external to Canada. Canadian governments and the business sector did have some initial concern about financial sector liquidity and the effects of a credit crunch on business large and small. However the major impact was on international commodity prices and international trade (especially with the USA), which drove down employment, profits, investment and, of course, government revenues (Cross, 2010). The overall economy declined by 3.6 percent over three quarters, the lowest drop among G-8 countries, and unemployment rose from 5.5 percent in late 2007 to 8.1 percent in late 2010, over half in the manufacturing sector. While all parts of Canada felt the effects, the downturn was most severe in Alberta (due in part to a sharp drop in oil prices) and in Ontario, particularly in the automobile manufacturing sector (Cross, 2010; Finance Canada, 2009). And of course, the recession had an immediate impact on public finances due to declining revenues and rising costs related to unemployment and welfare, an overall loss of about $20 billion (TD Economics, 2009).

In national political terms, the Harper government’s initial fiscal response to the international crisis and ensuing recession came in the ill-fated November 2008 statement soon after a general election in October. A political crisis for the minority Conservative government followed. The Opposition Liberal, Bloc Québécois and New Democratic parties all claimed that the statement did not meet the needs of the economic crisis, in particular that the policy response was insufficiently large or bold in terms of economic stimulus. They threatened to bring down the government and replace it with a left-centrist coalition, possibly forcing an election. Prime Minister Harper instead obtained the proroguing of Parliament to forestall a vote against his government, and bought more time to consult upon and prepare a new budget for late January 2009 (MacKinnon, 2009; Malloy, 2010). The “Economic Action Plan” passed by Parliament mainly through budget measures and associated legislation in 2009, and updated in subsequent annual budgets, restored the Conservatives political credibility in general, smoothing the way to their re-election as a majority government in May, 2011.

The Conservatives’ “Economic Action Plan” pumped nearly $40 billion of stimulus spending into the economy over two years and leveraged a further $11.6 billion in provincial and municipal spending as part of the conditions of intergovernmental grants (Finance Canada, 2009, Budget table 1.2). The total spending package was estimated by Finance Canada to be 3.2 percent of GDP, the second largest among G-7 countries, after the United States at 5.7 percent (Finance Canada, 2009, Budget table 3.2). The federal spending can be sorted into five categories. First is the “extraordinary financing framework” to assist the financial sector to ease

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5 Conlon and Posner (2010) note the significant increase in federal spending on an annual basis to State and Local governments from $208 billion in 2006 to $650 billion in 2010.
credit for individuals and businesses. Second is jobs-transition funding for individuals temporarily or permanently unemployed. Third is tax relief for house buyers and home renovators. Fourth is spending on public infrastructure, both directly by federal departments and joint funding with provincial governments (and through them in tripartite agreements with municipalities), aboriginal governments, and other partners. Fifth is sectoral adjustment funding for hard-hit industries (mainly auto), regions, and communities. One should also note that, apart from increases to the infrastructure partnership transfers, federal budgetary policy neither cut nor increased the major intergovernmental transfer programs.

Among the provinces, the most significant development was that their budgets did not trim expenditures to close the huge gap in revenues caused by the recession. Instead, all but one province (Saskatchewan) ran a deficit in 2008-09, and all of them did the same the year after. Thus the Canadian provinces managed one of the strongest counter-cyclical responses to the GFC, one of the few federal systems where subnational governments were in a position to do so (Swiss cantons also played a major counter-cyclical role) (Ter-Minassian, 2010). In August 2010 TD Economics reported that the federal budgetary position had deteriorated in just two years from +$9.5 billion in 2007-08 to -$53.8 billion in 2009-10, and the net position of all the provinces and territories from +$11.3 billion to -$26.8 billion, in the same period (TD Economics, 2010). Among the provinces, historic debt legacies combined with the recession to produce significant differences, from Quebec with a debt of nearly 50 percent of GDP to Alberta with no debt at all, and in terms of budgetary deficit with Ontario having the most serious ongoing budgetary position (the highest annual deficit as a percentage of GDP, approaching 3.5 percent). All governments indicated that their policy was to restore their budgets to a balanced position within 2-4 years, although as of 2013-14 (five years later) less than half of the provinces had achieved that goal, although all of them have an improved situation compared with 2009-10. Due in part to the marked decentralization of the Canadian fiscal system, the provinces remain among the most heavily indebted subnational governments in the OECD at 45 percent of GDP on average (gross, not net debt), although when blending federal and provincial debt, Canada’s fiscal consolidation challenge does not look as steep. In fiscal year 2014-15, net budget balance of the total government sector is estimated at just below 1 percent of GDP, for the first time since 2008-09, and net debt at 62 percent of GDP (TD Economics, 2014; Blochliger, 2013).

Throughout the GFC the federal, provincial and territorial governments sustained a generally cooperative and functional relationship. Perhaps because all regional economies were impacted by the down-turn, there was no evidence of discord on the overall macroeconomic stance to be taken. As noted, all provinces undertook a similar degree of countercyclical budgeting in sync with the federal position; all participated readily in a major acceleration of existing infrastructure programs to stimulate the construction and related sectors. The provinces have not been thrilled with the conditional nature of the federal funds, but seemed to swallow their objections (Young, 2009).

**Australia**

As with Canada, the Australian economy is heavily integrated in the global economy, including its financial sector. However, the GFC had no discernible origins in Australia and its private financial institutions were not severely damaged by the difficulties in the sub-prime mortgage
markets. There was in fact no national recession, as negative growth occurred only in one quarter (4th in 2008), and barely any impact on employment. Still, Australia’s overall economic position remained vulnerable to loss of export demand globally, and there was concern in particular about China. Governments (and business) were thus convinced that a strong and swift program of economic stimulus would help to cushion Australia from the shock, and temporarily help its private sector to weather the storms of weakening external demand and global credit shortage (Garnett and Lewis, 2010; Anderson and Fenna, 2010).

The federal government introduced two stimulus packages, the first at $12.7 billion announced in November 2008, the second at $42 billion in January 2009. Together with softening revenues, these expenditures contributed to a dramatic reversal of Australia’s federal budgetary position, from a surplus of $20 billion in 2007 to a deficit of $55 billion by June 2010, or 4.4 percent of GDP (Garnett and Lewis, 2010). The States position changed much less dramatically, and indeed was insulated in part by federal transfer increases or, with respect to the major remaining unconditional transfer, essentially little change (see figures in Treasurer of Australia, Budget 2009-10, Budget paper No. 3). On the whole the States position was mildly counter-cyclical. While it is unclear what impact it had, the Federal Treasurer also announced in March 2009 a temporary program to guarantee State borrowing programs.

The majority of the stimulus spending in Australia was delivered directly by the Commonwealth (i.e. federal) government in the form of tax cuts and credits, an increase in home-buyers grants, and a home insulation program. However significant portions were delivered by the States or local governments according to intergovernmental agreement reached in early 2009. This included $19.4 billion in special purpose payments to the States for education, including a new infrastructural capital program named Building the Educational Revolution, and increases to other federal-state infrastructure programs. Much of the new expenditure came with new layers of centrally mandated accountability measures. The $3.7 billion home insulation program and the $161.2 billion BER both received strong criticism for waste, delays and corruption, which seems to have been due to hasty roll-out and excessive central interference, among other problems (Kayrooz and Parker, 2010; Kortt and Dollery, 2012).

In political terms, the overall issue of economic stimulus – i.e. the wisdom of a Keynesian response – did not elicit much debate, certainly not from the States (where there emerged other more pressing concerns with the federal government unrelated to the GFC, including over health funding and reform, resource revenues and climate change) (Anderson and Parkin, 2010). The federal opposition was mainly content to blame the ALP government under Prime Minister Kevin Rudd for using the GFC as an excuse to ramp up unrelated Labor party policies, including education and the environment, and certainly made the most of the implementation fiascos of certain aspects of the stimulus programs. By 2010, when Julia Gillard replaced Rudd as ALP leader and won a (reduced) national electoral mandate, the GFC and

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Rudd’s somewhat risky commitment to a bold stimulus package were forgotten (Wanna, 2010). And as discussed below, the GFC response in Australia has been judged by some observers as reinforcing and legitimizing the centralization of the federal system, even while further entrenching collaborative process.

Finally, on the issue of fiscal consolidation, Australian states are among the most indebted among OECD countries, but at only about 6 percent of GDP the problem seems very small in comparison to the US states and Canadian provinces. The federal government also remains in deficit, at near 1 percent of GDP in 2014-15, and its debt has mounted, to peak at 33 percent of GDP in 2013-14 (net debt at 14 percent) (Treasurer of Australia, 2014: Budget Paper 1).

National Coordination and Intergovernmental Relations
To reiterate, explicit efforts at coordination in federal systems occurs mainly at two sites in the political process: the national (central) legislature and/or executive-dominated intergovernmental institutions. Occasionally the courts, through judicial review of statutes, or the resolution of constitutional disputes, will issue judgments that have the effect of imposing a coordinative solution on governments and private actors alike. Here we concentrate on the constitutional constraints, federal culture and other factors that shape the possibilities of national legislative action and intergovernmental outcomes, and then compare and assess what happened in 2008-13.

The constitutional constraints of federalism help shape policy coordination responses. The literature stresses the distribution of legislative powers between federal and subnational governments as well as the separate executive powers of each order of government (Watts, 2008; Hueglin and Fenna, 2005). Subnational power is protected and substantial in all three federal systems under review here but is often compromised by such factors as weak fiscal and administrative capacity, by central legislative pre-emption and by political and economic pressures for harmonization. Intergovernmental institutions, whether formalized or not, provide an important avenue for taming the pressure for centralization or for coordinating diverse policy initiatives and programs, including building consensus towards common objectives.

In the three federation set examined here, all of them have substantial fiscal autonomy; their federal systems as a whole are judged to be on the decentralized end of the spectrum (Shah, 2007; Anderson, 2009). Two of the set –Canada and Australia—have major systemic commitments to achieving equity in the fiscal capacity of states or provinces, in part as a way to promote national standards in policy outcomes. Fiscal transfers are especially significant in Canada given that the provincial legislative autonomy has been more strongly contained, i.e. national legislative and regulatory schemes cannot routinely preempt provincial ones, as they can in the United States and Australia.

Along with federal institutions and processes, prevailing political culture, including support for federalism values, are an important variable in explaining outcomes. A key aspect of federal culture is the degree of acceptance and support for constituent unit autonomy and, related

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7 This paper does not compare judicial outcomes affecting policy response to the financial economic crisis.
to that, tolerance for decentralized and diverse policy outcomes. Of the three examined here Australia is clearly the least accepting of the need for preserving state autonomy and the least tolerant of diversity, and conversely provides the strongest support for national integration, for strong forms of coordination, and for uniform policy results (Painter, 1998; Brown, 2002). The notion that any national legislation could intrude too far on state autonomy would occur to very few Australians.

The two North American federations are much more decentralist in orientation. Canada has a more federal society than the United States, given the presence and role of the national francophone minority and the role played by Quebec as the champion of that national minority, but diversity and decentralization in the US is also highly valued, if not on minority nationality lines. These federal cultural differences help to precondition the federal systems to less or more appetite for national legislative activism in terms of intruding on traditional state/provincial spheres of responsibility. In the United States there appears to be acceptance that the national legislation should have the authority to act in the national interest, if need be, to vitiate state legislation (a much less acceptable proposition in Canada), but such action is of course dependent on the crucible of Congressional deliberation where state and local interests are powerfully represented and where as a result national action is often delayed or modified to better accommodate state and local interests, often including the administrative interest of one or many state governments. Thus, in both Canada and the United States, the jurisdictional scope of potential federal legislation and its intersection with state/provincial interests are important political considerations.

The federal culture shapes intergovernmental machinery and outcomes as well, most clearly seen in the differences between Australia and Canada. In the former, governments have agreed to very comprehensive intergovernmental machinery with working rules that enable effective co-decision, including the establishment of joint, binding regulatory regimes (somewhat akin to intergovernmental relations in the European Union). In Canada there is distrust and distaste for strong intergovernmental institutions, and the working rules are for loose consensus and lowest common denominator results; the system is rarely capable of producing joint regulatory schemes, for example (Bakvis et al, 2009). The mode of executive federalism in Australia tends to centralized, uniform and highly coordinated results, whereas the Canadian mode leads to arm’s length cooperation (more independence) and competition (Brown, 2002).

During the GFC there was some intense but not an unusual level of activity in established intergovernmental institutions at the ministerial and officials level. In Canada the federal Prime Minister met briefly with the provincial and territorial Premiers, but much of the top-level meeting occurred on a bilateral basis. This minimalist approach reflects Prime Minister Harper’s distrust of entangling executive federalism, but may also have been appropriate in view of the widespread political consensus on the need for an ambitious set of stimulus measures and the fact that the main intergovernmental measures involved long-standing programs (Brown, 2010). In Australia existing executive federalism machinery was also employed, including the heavily institutionalized Council of Australian Governments (COAG). Federal Prime Minister Kevin Rudd was, in 2008-09, still strongly committed to a renewed use of COAG and other intergovernmental mechanisms (Anderson and Parkin, 2009).
The American system is not as directly comparable due to the separation of executive-legislative functions, inducing what has been called a matrix style of intergovernmental relations. Their typical results may be characterized as being more flexible, more bilateral and regional in scope, and focused more on administrative accommodation of federal schemes with state implementation preferences and realities (Bakvis and Brown, 2010; Cf. Stephens and Wikstrom, 2009). The federal response to the GFC and the recession is notable among recent policy cases in the United States for the substantive and symbolic substance of federal-state consensus-building. President Obama met at least annually with the National Governors Association and in recent years quite frequently with groupings of Democratic governors. This explicitly intergovernmental activity was in addition to the intense and more common practice of direct lobbying of Congress, the White House and federal administrative agencies by State Governors, legislators and senior administrators, as well as by state and local government associations based in Washington, D.C.

Competitive Processes
As introduced above, federal theorists, including scholars of fiscal federalism, suggest that policy coordination can be achieved not only through centralized or cooperative and collusive processes, but also—if somewhat directly—through competition. Inter-jurisdictional competition can be both state-to-state (horizontal) or federal-state (vertical), or both at the same time. It can be destructive, such as predatory or dumping kinds of behaviours, and in the case of standards, a downward harmonization, i.e. a “race to the bottom”. Or it can be creative, entailing experimentation, emulation and upward harmonization, i.e. a race to the top (Vogel, 1995; Rom, 2006; Harrison, 2006). The horizontal interprovincial competition represents the most obvious setting in that one is comparing governmental action at the same level, and citizens, political elites and other actors can most readily apply the lessons to be learned from their neighbours. Such competition can never be considered to be on a level playing field, however, given differences in territorial size, population, wealth, and fiscal and administrative capacity among the constituent units of any federation.

Federal-state or vertical competition suggests that voters, elites and policy communities can “forum shop” to achieve results (or to block results as the case may be). The complications arise in that the federal government almost always has more resources to bring to the game, even if obtaining sufficient political consensus to deploy those resources is not always present. Also, depending on the policy instrument employed, federal actions can trump state ones, seen most clearly in regulatory matters. Taxation and expenditure programs may be less conflictual in legal terms, but there remains much potential for harmful duplication.

Moreover, the federal culture discussed above affecting national legislative and intergovernmental relations also impacts upon the scope and effectiveness of competitive federalism. Canada, with its strong support of provincial autonomy provides fertile ground for competitive federalism. When governments cooperate they most often do so at arm’s length, pursuing collaboration from separate program bases, seeking only to obtain mutual adjustment among provinces and with them and the federal government. Canadians have a high tolerance for diverse policy outcomes and only rarely demand uniformity across the provinces. The notion of a strong national government pursuing and if need be imposing national standards is not an accepted fact, as it would be in the United States and Australia, but is, instead, a matter of

8 See references cited in note 2 above.
considerable contestation, including the existence of significant differences on this point among the federal political parties. It is significant that the Conservative government now holding office in Ottawa is committed, in broad terms, to what has been termed a “classical” approach to federalism, entailing an acceptance of competition and decentralization.

Such partisan differences also exist in the United States and Australia, at least historically, but evidence suggests that in the past twenty years or more that these two main parties in each case are converging (Posner, 2007; Anderson and Parkin, 2010). As noted Australia has highly coordinative intergovernmental relations which leave much less room than in the other two federations for competitive federalism. In the United States the State governments are generally much freer to pursue their own thing in many fields because national governments cannot find the political consensus to act, or indeed find virtue in the lack of an overarching national policy framework.

In all three federations, the state/provincial governments have autonomous budget policy, regardless of how dependent they are, collectively or individually, on transfers from the federal government. Moreover, budgetary policy remains a core test of effective governance and political survival. Responding to the GFC and recession nonetheless has its limits as a case of competitive federalism at work. Policy responses were by definition in the crisis mode, being quick fixes to swiftly moving events. There was little time to stabilize or optimize public finance once the economic slide had begun. This limits the creativity of governance or at the least means that governments have less room to move. The logic of the desirable scope of counter-cyclical policy would also, unlike other policy areas such as environmental regulation or social policy reform, militate against decentralized solutions. In a global financial crisis the urgency and salience of market discipline (even where the policy is to respond to market failure!) also would limit experimentation.

Pending a more thorough empirical review of subnational government policy outcomes, but based on an initial sounding of the literature and some aggregate data9, our conclusion is that the competitive context leads in this case to large elements of decentralized response but which still exhibit a strong convergence with national policy in all three federal systems, despite the rather sharp partisan and ideological divisions in the USA. This unforced coordination reduces the burden that would otherwise be borne by national integrative processes.

Conclusions
Let us return to the two propositions set out in the introduction. The first was that the more integrative the federal system, the more readily it will achieve effective policy coordination. The second was that policy coordination can be achieved through competitive processes as much as through cooperative or collusive practices. The case of the response to the GFC and global recession illustrates only partial confirmation of these propositions. Australia as the most theoretically and historically integrative of the three federations would be predicted to achieve the most impressive degree of policy coordination. However public finances in Australia both before, during and after the GFC have been much healthier than most OECD countries, certainly more so than Canada or the USA, which reduces intergovernmental complications. The main job was one of delivering federally-determined stimulus programs. Meanwhile, the United States, with its integrated party system, and stronger executive and legislative ability to act on the

9 See Ter-Minassian and Fedelino, 2010; Blochliger, 2013.
national interest, would in theory also be a candidate for a high degree of federal integration. And indeed this seems to have occurred most effectively during the middle phase of US response, i.e. after the election of November 2008 until early 2010 when there was a significant degree of bipartisan consensus, most notably around the ARRA. Canada, with its non-elected and arguably non-representative Senate, legally more autonomous provinces, and much weaker party integration than the United States and Australia, is in theory the least able to achieve national policy coordination. Yet in practice, in this case, Canada achieved the highest degree of coordination. This was not due to an intrusive set of national guidelines or legislation, nor to any new intergovernmental agreement. Rather important factors seem to be first, a generally high level of political consensus (regionally and in partisan terms) on the objectives and scale of economic stimulus and, second, heavy reliance on proven, existing intergovernmental fiscal and administrative mechanisms.

As for competitive federalism, it is bound up in the core fiscal federalism features and evolved public finance profiles of each country, i.e. highly predetermined by recent history in each state or province (or, for that matter, local government). In the USA most states and local governments had little room to manoeuvre to respond on their own, at least in the short term, to the GFC. Indeed the most significant response was to work with Washington on the joint measures. It appears that this situation relaxed considerably as the urgency of the GFC and global recession waned. In the more medium term challenges of fiscal consolidation, more room for diversity of response is available. Canadian provinces and, to a lesser extent, Australian states had more fiscal capacity, more policy manoevrability, and critically, stronger fiscal positions at the outset.

Finally, one may return to the four benchmarks for effective policy coordination set out in the second section of this paper: 1) The collective provision of sufficient economic stimulus to stabilize the national economy, relevant to the severity of the external shock and the impact and depth of recession; 2) Synchronicity of overall national macroeconomic efforts between the central and subnational governments, and among the subnational governments; 3) Flexible adjustment as required to intergovernmental fiscal arrangements; and 4) Consensus on longer-term fiscal consolidation. Figure 1 provides an overview of my assessment of these four benchmarks as applied to the three federations.

<table>
<thead>
<tr>
<th>Figure 1</th>
<th>Canada</th>
<th>USA</th>
<th>Australia</th>
</tr>
</thead>
<tbody>
<tr>
<td>1: sufficiency of collective stimulus?</td>
<td>Yes</td>
<td>In part</td>
<td>Yes</td>
</tr>
<tr>
<td>2: synchronized macro impact?</td>
<td>Yes</td>
<td>No</td>
<td>Mostly</td>
</tr>
<tr>
<td>3: flexible fiscal relations?</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
</tr>
<tr>
<td>4: Consensus on fiscal consolidation?</td>
<td>No</td>
<td>No</td>
<td>No</td>
</tr>
</tbody>
</table>
The sufficiency of collective stimulus in **benchmark one** is going to be in the eye of the beholder to a point, but general economic assessment would support the conclusion that stimulus measures in Australia and Canada helped to both reduce the length and depth of the recession (cite). In the United States there remains debate about whether the stimulus was fully sufficient given that recovery remained weak until 2013, and that pro-cyclical fiscal policy by state and local governments partly offset national measures.

On **benchmark two**, only Canada exhibits a fully synchronized macroeconomic policy stance, at least for the short-term crisis, among the federal and provincial governments. The United States is in general not able to attain such synchronicity given the constitutional and other constraints on deficit financing, although clearly states such as California were able to finesse their fiscal position for many months, delaying expenditure cuts and revenue cuts until a degree of private recovery had begun. In Australia, the States have a general ability to undertake a countercyclical fiscal stance, and most of them did do so to some extent, although they left most of the heavy lifting to the federal government.

On the flexibility of fiscal arrangements, **benchmark three**, design theory of federalism strongly suggests that fiscal federalism arrangements by being medium-term in duration and often with few constitutional constraints, provides an important measure of adaptability to change for federal systems. This case bears out that prediction in all three federations. An integral part of the US response was in fact to temporarily increase federal program transfers to the States and local government at a time when their fiscal capacity was badly damaged. To a degree, some of those programs also incorporated automatic stabilizers. In Canada’s case the flexibility was more selective. Although the federal government did not make matters worse for the provinces, it left much of the gap-filling to provincial deficit financing. However, on a horizontal equity basis, the fiscal equalization program continued to play an important role in stabilization. In Australia it is a bit more difficult to separate out fiscal arrangements reform that took place simultaneously with stimulus transfers, but clearly increasing transfers overall helped to shield State finances from the downturn.

Finally, on **benchmark four**, consensus on fiscal consolidation, none of the federations have achieved this goal. It is no coincidence that all three systems are relatively decentralized in fiscal terms among federations, and that state or provincial budgetary autonomy is well established. Moreover, despite some degree of adoption of fiscal rules (hard budget constraints) in some individual governments, there is both political and intellectual opposition – and certainly no positive consensus -- in all three countries to the idea of nationally binding fiscal rules or even targets for fiscal consolidation. That said, competitive market discipline is an important factor in all three and can be expected over time to exert considerable pressure on outlier governments.
References


Treasurer of Australia (2014) Budget Paper No. 3 Federal Fiscal Finance (Canberra)


