

Heads-of-Government Summit Institutionalization in Canada & Australia: Economic Liberalization and the Incentive to Cooperate

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Dedicated to the memory of
The Honourable
John Charles Bannon, AO, PhD
1943-2015

Premier of South Australia, 1982-1992
Visiting Research Fellow at Flinders University

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ABSTRACT

This study asks why Australia institutionalized its intergovernmental relations at the strategic, head-of-government (HoG) level whereas Canada did not. In the early-1990s, both federations undertook intergovernmental negotiations to redesign their respective economic unions, which were increasingly exposed to world economic shifts. The economic reform process engages what is referred to as the mechanism of continuous negotiations (see Imbrogno, forthcoming). Subsequent to these negotiations, Australia founded the Council of Australian Governments (COAG), an institutionalized HoG meeting. In contrast, Canada's economic reform effort – referred to as the Agreement on Internal Trade (AIT) – did not yield institutionalized First Ministers' Conferences (FMCs).

I argue that the political economy of each country, measured by their external market integration, impacted actors' behaviour and determined whether or not the mechanism of continuous negotiation was able to expand the economic reform process to include IGR institutional reform. The political economy is an understudied variable in the IGR literature. Through archival and interview evidence, the dissertation establishes the importance of the political economy variable in relation to alternative explanations, such as partisanship, party system, and vertical fiscal imbalance.

In the 1980s and 1990s, Australia's external market integration shifted from concentrated to diffuse, i.e. its exports shifted from the West toward a multitude of Asian trading partners. The risk inherent in this shift was coupled with an economic crisis in Australian growth, debt, employment, and current account balance to produce an incentive for leaders to cooperate on economic reforms. The result was continuous negotiations on economic reform during a series of HoG summits that successfully concluded economic reforms. These negotiations eventually expanded to include IGR institutional reform in order to secure the reform effort, thus founding Australia's peak IGR institution, COAG.

During the same time period, Canada also experienced an economic crisis in its growth, debt, employment, and productivity. The Canadian response was twofold: reform the domestic economy through constitutional reform and negotiate a free trade agreement with the United States. When the former process failed, leaders were forced into intergovernmental negotiations to achieve domestic reform in the face of the economic crisis and the added need to adjust to USA free trade. However, when the mechanism of continuous negotiations was engaged by HoG, economic reforms were not forthcoming nor did the negotiations expand to include IGR institutional reform. In the Canadian context, concentrated external market integration with the USA produced an incentive to compete between actors. Provinces sought to retain maximal economic policy autonomy by appealing to regional development policies, seeking exemptions to internal trade rules, and refusing to expand negotiations to include IGR institutional reform. FMCs thus remain weakly institutionalized.

RÉSUMÉ

Cette étude questionne la raison pour laquelle l'Australie a institutionnalisé ses relations intergouvernementales au niveau stratégique des chefs de l'administration (*heads-of-government* : HoG), alors que le Canada ne l'a pas fait. Au début des années 1990, les deux fédérations ont entrepris des négociations intergouvernementales pour repenser leurs unions économiques respectives, qui ont été de plus en plus exposées aux changements économiques mondiaux. Le processus de réforme économique engage ce qui est désigné comme étant le mécanisme de négociations continues (voir Imbrogno, forthcoming). À la suite de ces négociations, l'Australie a fondé le Conseil des gouvernements australiens (*Council of Australian Governments* : COAG), une réunion d'HoG institutionnalisée. En revanche, les efforts de réforme économique du Canada – appelés Accord sur le commerce intérieur – n'ont abouti sur aucune conférence institutionnalisée de premiers ministres (*First Ministers' Conferences* : FMCs).

Je soutiens que l'économie politique de chaque pays, mesurée par leur intégration sur le marché externe, a eut un impact sur le comportement des acteurs et a déterminé si le mécanisme de négociation continue fût en mesure d'élargir le processus de réforme économique pour inclure une réforme institutionnelle des relations intergouvernementales (IGR). L'économie politique est une variable peu étudiée dans la littérature traitant des IGR. Grâce à des preuves tirées d'archives et d'entrevues, mon travail établit l'importance de la variable de l'économie politique par rapport à d'autres explications, telles que la partisannerie, le système de partis, et le déséquilibre fiscal vertical.

Dans les années 1980 et 1990, l'intégration du marché extérieur de l'Australie est passée de concentrée à diffuse, c'est-à-dire que ses exportations se sont décalées de l'Ouest vers une multitude de partenaires commerciaux asiatiques. Le risque inhérent à cette évolution, couplée à une crise économique dans la croissance, la dette, l'emploi et le solde du compte courant incite les dirigeants à coopérer sur les réformes économiques. Le résultat prit la forme de négociations continues sur la réforme économique, au cours d'une série de sommets HoG qui ont conclu avec succès des réformes économiques. Ces négociations se sont finalement élargies pour inclure la réforme institutionnelle des IGR en vue de garantir l'effort de réforme, fondant ainsi l'institution IGR la plus élevée d'Australie, COAG.

Au cours de la même période, le Canada a également connu une crise économique dans sa croissance, sa dette, son emploi et sa productivité. La réponse du Canada était double: réformer l'économie nationale grâce à la réforme constitutionnelle et négocier un accord de libre-échange avec les États-Unis. Lorsque l'ancien processus a échoué, les dirigeants ont été contraints à des négociations intergouvernementales pour parvenir à une réforme interne face à la crise économique et à la nécessité grandissante de s'adapter au libre-échange des ÉU. Toutefois, le mécanisme de négociations continues n'a pas produit les réformes économiques et ne s'élargirent pas pour inclure la réforme institutionnelle des IGR. L'intégration concentrée du marché externe du Canada avec les ÉU a produit une incitation à la concurrence entre les acteurs. Les provinces ont cherché à conserver une autonomie maximale de la politique économique en faisant appel à des politiques régionales de développement, à la recherche de dérogations aux règles de commerce interne, et en refusant d'étendre les négociations afin d'inclure la réforme institutionnelle des IGR. Les FMCs restent donc faiblement institutionnalisées.

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ABBREVIATIONS

General

DVDependent Variable
EEC/EC/EUEuropean Economic Community/European Community/European Union
FOI	.....Freedom of Information
GATT	.....General Agreement on Tariffs and Trade
HoG	.....Heads-of-Government
IGR	.....Intergovernmental Relations
OECD	.....Organization for Economic Cooperation and Development
PM	.....Prime Minister
R&D	.....Research and Development
UN	.....United Nations
USD	.....United States Dollar
USA	.....United States of America
VFI	.....Vertical Fiscal Imbalance

Canadian

AIT	.....Agreement on Internal Trade
AB	.....Alberta (Edmonton)
BC	.....British Columbia (Victoria)
CBC	.....Canadian Broadcasting Corporation
CMA	.....Canadian Manufacturers' Association
CMIT	.....Committee of Ministers on Internal Trade
CoF	.....Council of the Federation

FMC	.....First Ministers' Conference
FMM	.....First Ministers' Meeting
FTA	.....Free Trade Agreement (between Canada and the USA)
ISTC	.....Industry, Science and Technology Canada, Ministry of
ITS	.....Internal Trade Secretariat
MB	.....Manitoba (Winnipeg)
MP	.....Member of Parliament
MPP	.....Member of Provincial Parliament of Ontario
MLA	.....Member of the Legislative Assembly
MASH	.....Municipal, Academic, Social Services and Hospitals
NB	.....New Brunswick (Fredericton)
NDP	.....New Democratic Party
NFLD	.....Newfoundland and Labrador (St. John's)
NAFTA	.....North American Free Trade Agreement (between Canada, USA, and Mexico)
NS	.....Nova Scotia (Halifax)
ON	.....Ontario (Toronto)
PEI	.....Prince Edward Island (Charlottetown)
QC	.....Québec (Quebec City)
SK	.....Saskatchewan (Regina)
SUFA	.....Social Union Framework Agreement
UPSUnited Postal Service

Australian

APECAsia Pacific Economic Co-operation
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ASEANAssociation of Southeast Asian Nations
ANZACAustralian and New Zealand Army Corps
ABC	.....Australian Broadcasting Corporation
ABS	.....Australian Bureau of Statistics
ACT	.....Australian Capital Territory (Canberra)
AUD	.....Australian Dollar
ANU	.....Australian National University, Canberra
COAG	.....Council of Australian Governments
CAF	.....Council of the Australian Federation
DPC	.....Department of Premier and Cabinet
DPMC	.....Department of Prime Minister and Cabinet
EPAC	.....Economic Planning Advisory Council
NLA	.....National Library of Australia
NPC	.....National Press Club of Australia
NSW	.....New South Wales (Sydney)
NZ	.....New Zealand
NT	.....Northern Territory (Darwin)
QLD	.....Queensland (Brisbane)
SA	.....South Australia (Adelaide)
SPC	.....Special Premiers' Conference
TasTasmania (Hobart)
VicVictoria (Melbourne)
WAWestern Australia (Perth)

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INTRODUCTION

Chapter 1

A neat and tidy mind is a crippling disability in understanding Canadian federalism.¹

Professor Ronald L. Watts, 1929-2015
(paraphrasing Professor James Alex Corry, 1899-1985)

¹ See Watts (1992, p. 13).

Federal political systems have unique difficulties with governance owing to the constitutional entrenchment of two sovereign orders of government. As more countries adopt federal political arrangements as the solution to various problems, the ability of federal systems to govern effectively has attracted significant attention. Increasingly, they must contend with forces of globalization and localism, which push and pull at the relations between the orders of government – the very fabric of federal governance. The health and well-being of these systems is evident by how governments adapt and adjust to these forces (Burgess, 2011). Adaptation and adjustment rely on processes of innovation. Since federal systems by definition have similar characteristics, an important question to consider is why similar systems innovate and change in different ways? Understanding the dynamics of federal institutional innovation and change is the goal to this dissertation.

As Ronald Watts argued, intergovernmental relations (IGR) is an inevitable force in federal politics.² It is also key to the ability of federal systems to adapt and adjust to external pressures. An IGR system has both formal and informal components and operates within every political system, whether it be unitary, federal, confederal, or multi-level. The study of IGR contained herein is concerned with its operation in federal parliamentary democracies. These countries experience significant pressure on their governance capabilities due to globalization, internationalization, liberalization, and localism, all of which have helped to spur the multi-level governance phenomenon.³ What are the impacts of these forces on IGR systems and institutions? Does change tend toward centralization or are federal systems being forced to decentralize? Or

² See Agranoff (2011) for a review of Watt's work on IGR.

³ See Piattoni (2010).

are these systems shifting horizontally into the grey area of multi-level governance, which emphasizes informal actor networks rather than legal and constitutional arrangements? Answering these questions adds to the literature on comparative federalism and contributes to the debate on whether or not IGR institutional change is affected by external factors.

This dissertation examines IGR institutional change in two federal democracies: Canada and Australia. It asks why Australia underwent significant IGR institutional change whilst Canada did not. Whilst the events under scrutiny in each case study occurred in the late-1980s and early-1990s, the issue of IGR system capacity is a timely topic.

Media observers regularly lament the state of IGR in Canada. Antonia Maioni (2015) wrote an op-ed in *The Globe and Mail* on the need for federal-provincial engagement at the highest level to produce “strategies on key issues that shape Canada’s future”. The editor of *The Walrus* lamented Canada’s outdated constitution in the face of globalization: “The country is trapped in a constitutional status quo,” opined J. Macfarlane (2012). If that is so, and if Watts (2008, p. 120) is correct that attempts at mega-constitutional politics are now redundant, then adapting to globalization falls to the purview of the IGR system and its quiet constitutionalism – the ability to change the constitution via intergovernmental agreements (McBride, 2003). Quiet constitutionalism enhances the adaptability and endurance of federal political systems hence why meetings of heads-of-government (HoG) are usually front page news and why the topic of multi-level governance is becoming an attractive tool with which to study federalism.

Because Canadian First Ministers’ Conferences (FMCs) – or the less formal First Ministers’ Meetings (FMMs) – have not been held consistently for some time, meetings of the Premiers, whether bilaterally or multilaterally, have garnered the spotlight. In 2015, Philippe Couillard of

Québec (QC) was the first Premier of any province in 50 years to speak before MPPs in Toronto. In his speech, he reinforced the view that Ontario (ON) and Québec are “natural allies. Central Canada is an economic force. It is a political force” (Csanady, 2015). To that effect, Ontario and Québec have held joint cabinet meetings and signed several bilateral deals, including reinstating access to public procurement to companies from either province. Here is evident one manner by which Canada adapts to new economic realities: bilateral negotiations. Yet the question remains why Canadian governments undertake a bilateral approach to reform rather than one that includes all jurisdictions?

The question is particularly relevant since only HoG meetings are capable of addressing national issues involving all policies and jurisdictions. Under newly-elected Prime Minister (PM) Justin Trudeau, all Canadian HoG met in November 2015 to discuss the Paris climate change talks and in March 2016 they reconvened to consider a national climate policy framework. Such meetings “serve the long-term interests of Canada” (Anderson, 2012). Yet FMMs of this nature have been rare in the last decade, opening a space for Council of the Federation (CoF) meetings to provide strategic policy leadership. At its 2015 meeting, the CoF released several news items on its activities:⁴ producing a shared vision and common principles for cooperation in energy policy; discussing the importance of joint action to combat climate change; acknowledging the work of the Health Care Innovation Working Group; lamenting the decline in federal funding for housing; urging the federal government to work with provincial ministers on an emergency management framework; signing a protocol on mutual recognition of apprentices; and

⁴ For all news releases, see Council of the Federation (2015).

announcing the creation of an Economic Productivity and Innovation Working Group to identify opportunities in these areas.

The contrast between ON-QC bilateralism, recent FMMs, and the CoF is important. Bilateralism produced specific policy changes whilst both kinds of multilateralism considered a more expansive list of policies but contained fewer concrete policy changes. As a whole, Canadian IGR remains mostly stuck in the early stages of policy-making, analysis and investigation, which places a heavy burden on bilateralism. Part of the problem has been the relative absence of the federal government at these meetings in recent years. Andrew Coyne (2013) considers that at CoF meetings, the Premiers never discuss policies within their own jurisdictions, “instead, they talk about the feds...[and] when they are done writing Ottawa’s budgets...and drafting federal safety regulations, and demanding to be consulted on everything under the sun – the premiers...complain about federal interference”. Less polemically, policies designed solely at the provincial level “without federal commitment or contribution...remain stymied [to the point that] Canada cannot properly function as a federation, even a decentralized one...without the active engagement of the federal government” (Maioni, 2015). Why did Canadian IGR adjust to globalization and liberalization in this way?

Maioni’s warning, Coyne’s lament, and Macfarlane’s observation in the national press indicate that there are problems with Canadian IGR. It is therefore incumbent on researchers to identify the problems and understand why they have emerged. One answer usually provided for the state of contemporary Canadian IGR is that former PM Stephen Harper simply did not want to attend HoG meetings (Fekete, 2015; McKenna, 2014; Wells, 2015). He dealt with the provinces bilaterally, and less publicly. This answer supports the idea that Canadian IGR is overly reliant on

political personalities (the Couillard-Wynne alliance can also be considered a result of personality characteristics, including their partisan predispositions and opposition to the then-Conservative federal government). Trudeau's 'sunny ways' and his re-engagement with the Premiers is also a product of his style of politics. But from an academic perspective, partisanship is not the only answer.

The personality factor does not completely account for the current state of Canadian IGR, which has steady declined over the terms of four different PMs from both governing political parties; the personality answer is not wrong but it is incomplete. The dissertation aims to provide a more complete answer, particularly one that goes beyond pure agency to include the economic and institutional setting. This may sound like a cumbersome and complex task but, to paraphrase the introductory quote from Watts and Corry, an understanding of Canadian federalism requires some imaginative thinking to discern reality.

The recent Canadian IGR experience today contrasts starkly with that of a federation with which it is often compared: Australia. Since 1992, Australia's more institutionalized IGR system has churned out policy after policy throughout its short history and during the terms of both governing parties. At a recent meeting in July 2015 – the 40th meeting of the Council of Australian Governments (COAG) – the PM and state Premiers agreed to a counter-terrorism strategy and revised the threat advisory system; heard expert advice on the campaign against violence for women; and determined to consider a strategy for dealing with hard drugs (Council of Australian Governments, 2015b). These issues were carried over from the 39th meeting in April, which also considered other policies, such as the roll out of the National Disability Insurance Scheme and the first review in 20 years of competition policy (Council of Australian Governments, 2015a).

Then at the very first Leaders' Retreat (held a day before the official meeting), HoG outlined an ambitious agenda to tackle a host of reforms so that governments "can cooperate more effectively to make major improvements in the delivery of services to all Australians [in the areas of] health, education, infrastructure and housing". They also supported the Northern Territory's (NT) resolve to become a fully-fledged state by 2018.⁵

Considering that Australia and Canada share so many political, economic, and social characteristics, explaining Canadian IGR's current status requires a direct comparison with Australia. Even the surface comparison of news releases and communiqués illustrates that these federal parliamentary systems have two very different IGR systems. Even the vocabulary of their peak IGR institutions are different: news releases versus communiqués. Canadian IGR is more informal and rhetorical – news releases are fleeting and carry few details. It is also more competitive, particularly since the Couillard-Wynne alliance is "an apparent effort to push back against the growing ascendancy of the west in Confederation" (Csanady, 2015). At the March 2016 FMM, Premier Wynne stated that "It is very, very important to us in Ontario that the partnership with Québec continue to be strengthened...it's important to Canada, I think, for Central Canada to be working together" (McParland, 2016). And of course there is the often testy relationship between Ottawa and various provinces at any given time. Canadian IGR is not routinized nor is it infused with much value; it is weakly institutionalized at the HoG level.

This stands in sharp contrast to Australian IGR, which is more consensual and cooperative and makes coordinated strategic decisions on national policies – communiqués are official documents meant to transmit decisions to political actors and institutions. After it underwent

⁵ See Australian Government (2015) for the Reform of the Federation White Paper.

significant change in 1992, Australian HoG summits became more routinized and infused with much more value; it is between medium and strongly institutionalized. Therefore, not only is there a difference in IGR system type (cooperative vs competitive), there is also a clear difference in the level of institutionalization of Canadian and Australian HoG meetings. Understanding why IGR is at its current state in both countries begins and ends with these meetings.

What accounts for the institutionalization of HoG summits? In Canada, scholars have focused on partisanship (Esselment, 2012), diverse federal society (D. Brown, 2002), and political factors – such as elections (Bolleyer, 2009; Simeon, 2006) and fiscal federalism (Turgeon & Wallner, 2013) – as explanations for its decentralized IGR system. The personalities of politicians (Dupré, 1985) and the characteristics of IGR officials (Inwood, Johns, & O'Reilly, 2011; J. Simmons, 2004) have also been investigated. These explanation are insufficient on their own to explain the observed outcome because they are unable to fully account for changes to the IGR system and for the timing of such changes. At one time, both Canada and Australia had competitive IGR systems despite differences in certain variables, such as party system integration and vertical fiscal imbalance. Is there a variable that helps account for both the change and its timing?

The dissertation introduces political economy as a plausible explanation for the variance between the two cases. Actors are influenced by many incentives yet prior studies have not directly connected economic incentives and reform processes to the operation of IGR systems. Brown's (2002, p. 265) study of Canadian and Australian economic reform is perhaps the closest comparable study because it analysed the same time period to conclude that federalism is "alive and well" in both countries. This dissertation advances his study by specifically addressing IGR institutional change (mentioned only briefly by Brown) and employing extensive use of archival

and interview data to analyse the connection between processes of economic and institutional reform.

The dissertation also offers strong insights into the debate on whether or not IGR institutional change is affected by external factors. On one side, Hale (2004) and Lazar, Telford, and Watts (2003) conclude that IGR systems remain largely untransformed by external economic sources. On the other side, as supported by this dissertation, is the argument made by Courchene (1995) contending that external economic pressures do indeed impact IGR systems. This idea is part of a broader contention that federalism itself is not necessarily an independent variable (see Hueglin 1990).

The dissertation contends that the institutionalization of HoG summits depends on the institutions and processes used to effect cooperation on economic liberalization. Embedded in the process of economic liberalization is the mechanism of continuous negotiation between the orders of government. The mechanism is significant because it is a vehicle for transmitting economic incentives into intergovernmental negotiations such that they may expand to include IGR institutional reform (see Imbrogno, forthcoming). The dissertation argues that when HoG engage an economic reform programme, incentives from the political economy condition whether actors turn continuous negotiations on economic reform into negotiation on reforming their IGR institutions.

In both Canada and Australia, internal trade is too small to produce on its own an overwhelming incentive to institutionalize. Thus, we turn to an examination of their external economies, which are drastically different. Canada relies on one dominant trade partner – the United States of America (USA) – whilst Australia trades with a multitude of partners who

emerged during the 1980s and 1990s, resulting in a dramatic shift in its export orientation from West to East. Australia faced declining terms of trade and an increased number of significant trading partners due to booming Asian markets. What became known as the 'turn to Asia', coupled with recession and economic crisis, produced economic risks that helped generate a cooperative incentive on domestic economic issues. Eventually, this instilled more cooperative IGR that helped institutionalize a HoG summit.

In the Canadian case, one dominant trading partner generates a competitive incentive between actors, encouraging them to secure as much policy manoeuvrability as possible in order to remain economically competitive vis-à-vis each other and the American markets within which they are heavily integrated. Regional development is a key policy with which provinces seek to diversify their economies and defend their policy capabilities in the face of national, multi-lateral reform efforts. In this scenario, cooperative IGR is not a priority and so neither are FMCs.

By examining each case in detail, the dissertation advances Brown's study of economic reform to include its impact on IGR institutional reform. The result is that unique events are generalized into variables and mechanisms that add to our understanding on processes of economic reform and IGR institutional change in federal systems.

The dissertation is composed of four parts. Part One outlines the methodology: a two-case study of Australian and Canadian IGR. The chapter then develops a theory that explains the institutionalization of HoG summits in multi-level systems and examines alternative explanations. More precisely, the chapter theorizes a process by which HoG summits institutionalize into meetings. Part Two and Three then apply process tracing to each case study, with a focus on HoG summits and microeconomic reform.

In Part Two, chapters three and four, the events and context surrounding the founding of COAG are investigated using primary research gathered during fieldwork in Canberra, Adelaide, Melbourne, and Sydney in the summer of 2014. Interviews were conducted with officials and politicians involved in the Special Premiers' Conference (SPC) process between 1990 and 1992 as well as with current officials responsible for organizing and running COAG meetings. Both former Prime Ministers from the time refused interview requests and so their testimony is extracted from archives, public speeches, biographies, television interviews, and documentaries. Interviews regarding past events were supplemented with archival material. The National Library of Australia (NLA), the State Libraries of South Australia, Victoria, and New South Wales, and the Public Records Office of Victoria contained invaluable material on the time in question. The Bob Hawke Prime Ministerial Library and the John Bannon Collection at Flinders University also generously provided documents. Freedom of information (FOI) requests were submitted to the Commonwealth Government and the state governments of Victoria, New South Wales, and the Australian Capital Territory.⁶ In addition, secondary literature encompasses a significant portion of research, which was accessed both online and in person at the State and National Libraries as well as at the libraries of the Australian National University, Flinders University, the University of Melbourne, and the Museum of Australian Democracy.

In Part Three, chapters five and six, Canadian HoG summits after the Charlottetown referendum are investigated using primary research gathered from interviews and archives throughout the country. Former Premiers and former Provincial and Federal Ministers were

⁶ The Commonwealth government whittled down the request to one file, whilst NSW did not respond. ACT responded but not within the 10 week timeframe of the fieldwork and therefore its archives could not be visited. The Victorian government was most accommodative with its files.

contacted for interviews, which were finally granted by provincial-level officials only. Archives in Ontario and Québec were visited several times during the research. Some files were available outright whilst others required permission for public access, hence the multiple visits. Owing to a lack of files at Library and Archives Canada, a FOI request was submitted to the Privy Council Office (PCO). They provided some Cabinet documents but directed me to submit a request to Industry Canada to garner more detailed files, which proved successful.⁷ A FOI request was also sent to the Alberta (AB) Department of International and Intergovernmental Affairs. Because the AB FOI office was seconded by the Ministry of Justice to investigate the alleged activities of former Premiers, the request was delayed by a year and was only received near the time of submission. Finally, McGill University, University of Ottawa, and York University libraries were accessed for secondary sources.

The last section, Part Four, chapter seven, concludes the study by elucidating the comparison's results and by analyzing their relevance to the theory as outlined in Part One. The implications and predictive potential of the study are also considered. It is hoped this analysis helps bolster "the comparative interest in Canada's messy, unorthodox, intergovernmental, multinational, and asymmetrical federalism" (Hueglin, 2014, p. 10).

⁷ Other FOI requests were sent to the Internal Trade Secretariat, which was ignored, and to the Canadian Intergovernmental Conference Secretariat, which was inconclusive.

PART ONE:

THEORY AND METHODOLOGY

Chapter 2:

Theory of Heads-of-Government Summit Institutionalization

*It is not easy to see how matters could be worsened by a parley
at the summit.⁸*

Sir Winston Leonard Spencer-Churchill
Prime Minister of the UK, 1940-1945, 1951-1955

⁸ Edinburgh, 14 February 1950 (Reynolds, 2005).

Why do the levels of institutionalization of HoG meetings differ amongst multi-level systems? More specifically, why do some multi-level political systems have highly institutionalized HoG meetings at the apex of their intergovernmental relations systems whilst others do not? In some systems, infrequent and irregular HoG summits are convened that have no formal operational rules whilst in other systems HoG meetings are situated at the top on an IGR decision-making pyramid and act as a key strategic decision-making forum.

The dependent variable under scrutiny here is the level of institutionalization of HoG summits. Both the concept, the institution, and their measures are investigated in the next section. Once defined, alternative theories that may explain HoG summit institutionalization are introduced. These alternatives dominate the literature, leaving open some room to investigate other explanations. Next, the political economy independent variable is introduced as a key part of the proposed theory of HoG summit institutionalization. The case studies that are used to test the theory are outlined in the last section.

Concepts of the Dependent Variable

Intergovernmental Relations

The institution under scrutiny here is the intergovernmental space where actors meet to make, apply, interpret, and enforce rules. A central purpose of these spaces is to enable actors to produce rules governing their subsequent interactions, particularly their policy-making activities (Sweet, Fligstein, & Sandholtz, 2001). The generic concept of intergovernmental spaces comes in a variety of forms, such as regional cooperation in Sweden (Mccallion, 2007) or the Memorandum of Understanding on Devolution (United Kingdom Government, 2013). The form specific to federal political systems is the IGR system. The IGR of federal systems is essentially a

system of complex and intertwined relations between officials from the orders of government endowed with sovereign powers (see Watts, 2003). Categorizing the myriad kinds of relationships that may exist within one IGR system has proven difficult. Scholars undertaking a systemic approach to studying IGR often attempt to provide “an overall picture of the patterns of IGR in a particular political system” (Bolleyer, 2009, p. 16). An amalgamation of IGR patterns was utilized by D. Brown (2002) to construct a typology of IGR systems. His typology includes competitive, cooperative,⁹ and rational IGR systems, which are differentiated by the behaviour patterns one finds in each system. Competitive relations value autonomy and liberty, cooperative relations value harmonization and problem-solving, whilst rational relations focus on efficiency and certainty. These values are witnessed in the tasks that IGR systems perform: 1) how each order of government comes to occupy policy fields; 2) how governments coordinate policies in the same field; and 3) the style by which policies are negotiated.

There are many intergovernmental spaces within an IGR system that perform these tasks and contribute to the system’s classification: HoG summits, ministerial councils, working committees, task forces, conference calls, and informal meetings. The dependent variable is especially concerned with how one IGR institution performs these tasks. The dependent variable is thus comprised of two parts: the nature of HoG summits and their level of institutionalization.

⁹ The Canadian literature has distinguished between cooperative and collaborative federalism (Meekison, Telford, & Lazar, 2004). The former existed in an era of federal government spending to expand the welfare state, when the provinces were largely administrators of policy. Eventually, executive and competitive federalism eroded this so-called cooperation. Provinces came to exercise their functions of co-equal policy-makers and agenda-setters within a system of collaborative federalism. Despite the difference between the terms, Brown’s cooperative category is essentially referring to collaborative federalism. Henceforth, the terms are used interchangeably.

Table 1: Typology of Intergovernmental Relations

<u>IGR system type:</u>	Competition	Co-operation	Rationalization
<u>IGR system task:</u>			
Policy field occupation	• competitive	• mediated	• consolidated & single
Policy coordination	• “unseen hand” of competition	• voluntary agreement	• mandatory consolidation
Style of negotiation	• unilateral thrust and riposte	• consensus or negotiated decision-making	• unilateral, unified decision-making

Source: D. Brown (2002).

Heads-of-Government Summits

By focusing on the changes that occur to a specific intergovernmental space as measured by its level of institutionalization, the dissertation investigates the factors that influence overall IGR system design. The following defines HoG summits and briefly investigates their origins, beginning with the founding document of all federal systems, the constitution.

Constitutions of a federal nature are equivocal documents that establish federal institutions and sub-state governments, enshrine them with certain powers, and outline the rules for acquiring political power. As Sartori (1997) noted, constitutions are not themselves destinations but provide the rules for someone with a destination in mind to attain power.

Constitutions are supposed to define governing institutions yet meetings of HoG were not conceived of when several multi-level systems were founded.¹⁰ In Canada, HoG meetings were not included in the *British North America Act* of 1867. In Australia, they were not a part of its

¹⁰ Indeed, “the written constitution of the Canadian federation is of limited use in explaining how the federal system works” (Erk, 2008, p. 55).

federation in 1901, and in the European Union (EU), HoG meetings were not officially included in the supranational decision-making process enshrined in the *Treaty of Rome* of 1958. As well, there are no required meetings of HoG in the *German Basic Law*, although Article 23 (5) and (6) describe the obligation of the federal government to consult the *Länder* regarding EU legislation. Federal-*Länder* relations take place in hundreds of different committees, some of which have formal legal status (Lehner, 1988).¹¹ Swiss meetings are a product of its history rather than the constitution (for example, the collegiality of the Federal Council),¹² although, as in Germany, Article 44 of the *Swiss Federal Constitution* stipulates that the cantons and centre government owe each other a duty of consideration and support. It also obliges them to negotiate when disputes arise, which has created “an elaborate system of federal-cantonal committees” though not as extensive or formalized as in Germany (Lehner, 1988, p. 211).

Switzerland, the EU, and Germany aside,¹³ where do the first summits originate if not the constitution? In Canada and Australia, current events and the political situation necessitated summits between HoG. Historically, these first summits were ad hoc, informal gatherings between sub-unit and centre leaders during which specific topics were discussed, mostly concerning redressing fiscal imbalances, and consensus sought on important issues, usually economic in nature.¹⁴ Yet these summits remained weakly institutionalized for some time, resulting in a less formal system of IGR. Subsequent events and important issues continued to be handled as they occurred in an ad hoc and informal manner, even when those issues required a

¹¹ See also Chandler and Zöllner (1986).

¹² See Alain-G. Gagnon (1991).

¹³ These are categorized as rational IGR systems and so are not included in this comparison.

¹⁴ For example, see Janigan (2012).

more systematic governance approach. The systematic approach was realized only after the demise of classical federalism, which is a precursor to HoG summit institutionalization.

The powers listed in a federal constitution are often defined broadly and, before the 20th century, were divided between orders of government in the belief that each could exercise their powers independently. This is dual or classical federalism (Wheare, 1963). Today, most constitutions continue to divide powers between orders of government¹⁵ yet the reality is that both are responsible for policy outcomes regardless of how powers are divided in the constitution. This is referred to most simply as interdependence. Governments now operate within a web of governance that includes multiple stakeholders and sources of inputs and feedback. In multi-level systems, the development of the welfare state and an increase in the speed of globalization demanded intergovernmental cooperation between constitutionally-sovereign powers (Agranoff, 2004; Watts, 2008).

The demand for intergovernmental cooperation originates in the fact that changes on the ground are far more difficult to enshrine in constitutions given the speed at which change occurs, the difficulty in drafting amendments, and the time required to approve them, especially considering that most federal systems require supermajorities for amendments (see Lijphart, 1999). Since continuously amending the constitution to suit changing technological, economic, or political conditions is impractical, it falls to the IGR system to manage the adaptation to new conditions (Watts, 2008). This occurred to such an extent that the concept of quiet

¹⁵ In Canada, the *Labour Conventions reference* of 1937 states that the powers of each order of government are 'watertight compartments.' The concept emerged when the federal government attempted to legislate in areas of provincial jurisdiction as a consequence of Canada's adherence to an international treaty. In Australia, the High Court initially sustained this view upon federation but eventually reversed it in the 1920 *Engineers' Case*.

constitutionalism was identified (McBride, 2003). Indeed, the field of federalism itself has changed from focusing on legal/constitutional analyses (Bowie & Friedrich, 1954; Livingston, 1956; McWhinney, 1962; Wheare, 1963) to understanding federalism as a complex system of interrelationships; a non-hierarchical policy matrix (Elazar, 1987) that has evolved from a dual 'layer cake' to a more complex 'marble cake' model (Grodzins, 1966). External pressures, changing conditions, and interdependence have in turn rendered the IGR system susceptible to change and adjustment in order to meet the needs of actors and voters. Therefore, if federal institutions are to change, then it is likely to occur via *and* to the IGR system.

The pinnacle of the IGR system is usually a meeting of all heads-of-government. It is here that all sovereign powers are exerted, which grants HoG meetings a special status within IGR systems; they are a different kind of meeting that is inextricably linked to every other intergovernmental space. HoG "have played a key role in articulating visions...[They] have a certain degree of freedom of maneuver [and] their freedom is greatest when they are the ones to construct the founding ideas of a given discourse" (Schmidt, 2012, p. 171). Through their visions and discourse they provide political impetus to policy issues and are uniquely qualified to craft multi-policy package deals. These package deals are political decisions on technical policy options as first developed by line ministries. Such decisions require tradeoffs that only HoG can decide upon. The ability to execute these tasks and make decisions in part depends on the design and rules of HoG meetings, i.e., on its level of institutionalization.

Before moving on to the second aspect of the dependent variable, there is an important caveat to this study of HoG summit institutionalization: it is assumed that a HoG summit has already been held at some point in the polity's history. That is, this dissertation does not seek to

explain the origins of HoG summits, which would necessitate its expansion beyond time and resource limits. Where this study of institutionalization begins is some time after a pattern of ad hoc, irregularly-timed summits has been established. Over time, these summits became highly institutionalized meetings, remained at their original lower level of institutionalization, or even disappeared altogether.

Institutionalization

What is institutionalization, how is it measured, and how does it affect political systems? Since HoG meetings are rarely if ever established by the constitutions, their design and operation are conditional on other factors. Thus, even when HoG summits are convened, their institutionalization is not automatic.

Huntington (1968, p. 12) defines institutionalization as “the process by which organizations and procedures acquire value and stability”. A polity’s level of institutionalization is measured by considering its adaptability, complexity, autonomy, and coherence. Since then, many scholars have debated whether these are appropriate measures of institutionalization. Emmerson (1986) argues that adaptability is the most convincing of Huntington’s four dimensions of institutionalization because complexity, autonomy, and coherence can all have either suboptimal or optimal results. For example, too much complexity in state institutions can lead to instability rather than stability and too much autonomy can unbind a state from its public, rendering it unresponsive. Adaptability remains a useful measure of institutionalization because, unlike the other measures, it is contingent on the context within which institutions operate. How institutions respond to environmental changes is indicative of their institutionalization. As Huntington (1968) states, an institution that has developed a life of its own becomes more

adaptable and is thus better able to survive in a changing environment; it is institutionalized if it exists over time. This is a binary measure of institutionalization: it either exists over time or does not. For example, the Canadian Senate has existed since 1867 despite the enormous changes that have occurred since. It is most certainly institutionalized.

Smock (1973, p. 5) describes political institutionalization as “a measure of the performance of a structure, not a description of organizational characteristics. Political institutionalization indicates the degree to which a structure has evolved toward performing effectively.” This is quite similar to adaptability, since an effective institution will most certainly be capable of adapting to changing circumstances. According to this view, institutionalization is not necessarily an internal characteristic of institutions nor of their existence over time but an indication of how an institution is related to other societal institutions. Including effectiveness is important for Smock since a political system may simply copy the rules of other more successful polities yet those rules may not necessarily be institutionalized to the same extent as they are in the original polity. For Smock (1973), regularization has the potential to produce effectiveness. Regularization is therefore a necessary but not sufficient condition for institutionalization. This leads to the comprehensive definition of institutionalization as employed by Scalapino (1986, p. 1), which he defines as “the process whereby a political structure is made operational in accordance with stipulated rules and procedures, enabling regularized, predictable patterns of political behaviour, minimal trauma in power transfer and a foundation for effective development of policies as well as the application of justice”.

However, there remains a problem with these definitions because they conflate the characteristics of an institution with its outputs. This is an important premise of

institutionalization. According to Huntington (1968), an institution infused with value is more adaptable and thus better able to survive in a changing environment. The premise is that effective institutions must also be highly institutionalized; as Churchill implied, what possible harm could come from holding a summit? The premise relies on interactions that yield productive outcomes, which induce participants to increase their commitment to the structure of said interactions (Ostrom, 2005): “A society with highly institutionalized governing organizations and procedures is more able to articulate and achieve its public interests” (Huntington, 1968, p. 24). An increase in participant commitment is also why cooperation is more likely to occur within a highly-institutionalized IGR system; greater routinization and high value infusion are conducive to mediated occupation of policy fields, voluntary agreement, and a consensual style of negotiation. Evidence supporting the premise regarding effectiveness and institutionalization is present throughout the literature (see for example Bolleyer, 2006; Kuhonta, 2011). But the purpose here is not to measure the effectiveness of institutions, rather it is to understand why institutionalization occurs in the first place. How to do this whilst remaining agnostic regarding outcomes?

Levitsky (1998) suggests that scholars distinguish more clearly between two types of institutionalization, to the point of treating them as distinct concepts. These are routinization and value infusion. Levitsky argues that such parsing is necessary because these concepts analyze different behaviours that do not necessarily occur together. In this formulation, a routinized institution can lack value just as much as a value infused institution can be informal and ad hoc. And neither of these concepts relies exclusively on effectiveness. Returning to the example of

the Canadian Senate, it is routinized but also derided within Canadian politics (for example, see Doherty, 2002).

Levitsky views routinization as patterns of regularized behaviour within an organization. They are regularized because “institutionalized rules and behaviour patterns come to be perceived by individual actors as permanent structures” (Levitsky, 1998, p. 81). Measuring routinization requires a list of criteria for measuring the level of institutionalization of intergovernmental arrangements (see Table 2). The measures are: the density of contacts between officials, the regularity of meetings, the presence of supporting institutions, the kind of decision-making rules (unanimity vs. majority voting), the level of internal functional differentiation (the number of tasks assigned to supporting institutions), the specificity of the agreements concluded, and finally, the legal status of agreements (Bolleyer, 2006). Generally, an institution is strongly routinized if all the criteria apply to it; institutionalization is more than simply meeting regularly. Therefore, Bolleyer’s criteria in Table 2 is used to measure the routinization aspect of institutionalization.

As Huntington (1968, p. 15) states, value infusion occurs when an organization can outlive the function that it was initially created to perform. In this instance, the organization becomes more than simply an instrument to achieve certain purposes and develops a life of its own apart from the specific functions it was created to perform. Levitsky (1998, p. 79) concurs, indicating that value infusion is when actors’ goals shift from the pursuit of particular objectives through an organization to the goal of perpetuating the organization itself. Institutionalization is not automatic, it has to be built by actors (Blondel, 2006). Measuring this requires assessing actors’ opinions of an organization or institution: is the institution an expendable tool for achieving their

goals or is it prized and valued? These measures deal with all facets of an organization, its functions, the actors' role and place within the organization, their relationship with other actors, and their own thoughts and feelings toward the organization. In management studies, value infusion involves measuring whether top managers appreciate the institution in question (Heugens, Kaptein, & Oosterhout, 2008; Schuler, Murtha, & Lenway, 2010). From this it is possible to develop certain criteria for measuring value infusion. These include the status of the institution, how defined are its roles and responsibilities, how embedded is it within the political system, how committed are actors to participating within the institution, and finally, the level of resources allocated to it.

At a glance, there is some overlap between some of the indicators in Table 2 and those described here, but this is to be expected. Taking the time to define an institution, establish its roles and responsibilities, and allocate resources to it convey that actors value an institution as well as indicate its routinization: "The investment in [specific competencies, resources and personnel] indicates that intergovernmental transactions do not only express a momentary interest convergence of a group of individual actors" (Bolleyer, 2006, p. 393). The point is that all aspects of institutionalization must be analyzed in order to provide a complete picture of it.

Thus we arrive at definitions and measures of institutionalization: routinization and value infusion. Routinization involves patterns of regularized behaviour that actors perceive as permanent. Distinguishing between levels of routinization is accomplished by using the criteria in Table 2. Value infusion involves actors seeking to perpetuate an institution as evidenced by the efforts they direct to that end, which are gathered from their statements and actions.

Table 2: Indicators for Degree of Routinization

<u>Measures of Routinization</u>	<u>Level of Institutionalization</u>	<u>HoG Meetings</u>
Density of contacts	Weak Institutionalization	1) Canadian FMCs/FMMs
Regularity of meetings		2) Australian Premiers' Conferences and Loan Councils (until 1992)
Autonomous organization <ul style="list-style-type: none"> - Own secretariat - Clearly defined functions - Formal basis 	Medium Institutionalization	3) Council of Australian Governments (1992-today)
Majority Rule		
Internal functional differentiation <ul style="list-style-type: none"> - Specification of offices - Specification of sub-units/bodies 	Strong Institutionalization	
Specificity of agreements		
Legal status of agreements		

Source: Bolleyer (2006). Placement of Canadian and Australian HoG meetings by author.

Australia and Canada

Now that the dependent variable and its measures are established, it remains to select the best cases for comparison. A viable comparison requires the cases to differ significantly with regard to the dependent variable – minor changes would make it difficult to conclude on the factors that influence change. The comparison's viability is strengthened when comparing cases that have similar measures for the dependent variable that then diverge to a significant degree. On that note, the following selects cases on the dependent variable and outlines why their

comparison is logical. But before moving onto case selection, a note about how to conduct process tracing in small-N case studies that seek to determine causality.

Process Tracing

To be theoretically relevant, a small-N case study requires a specific kind of evidence, namely, causal-process observations. These are “an insight or piece of data that provides information about context, process, or mechanism and that contributes distinctive leverage to causal inference” (Brady, Collier, & Seawright, 2006, p. 355). The process tracing methodology identifies causal process observations relating to causal factors, along with their transmission mechanisms, and follows their effects through time (Blatter & Haverland 2012, Bennett & Checkel 2015). The specific mode of process tracing employed here is explaining-outcome process tracing via the inductive path, which builds an explanation for complex, multi-factored events with mechanisms and supporting data (Beach & Pedersen 2013). By closely examining the events, decisions, and structural conditions that led up to the institutionalization of HoG summits in each case, the analysis contributes to explanations of summitry’s institutionalization.

Explanations based on causal mechanisms “provide a fine-grained and tight coupling between [dependent and independent variables]” (Hedstrom & Swedberg, 1996, p. 180). Mechanisms are the basic building blocks of middle-range theories. Their elucidation assists in increasing the causal leverage of process tracing-based narratives. The posited mechanism at work in the cases is continuous negotiation on economic reform, which emerges when HoG respond to changes in the global economy. This mechanism impacts the existing political system and, in combination with independent variables such as the political economy, determines whether or not change occurs. Its presence in one case and its lack of presence in the other case

prove to be significant factors of the observed outcomes. The overall result of this approach to causality is the completion of a detailed and comprehensive analysis of empirical data that supports theoretical contentions and produces interpretable and defensible answers to research questions (Brady, Collier, & Seawright, 2004).

Case Selection

The puzzle under investigation concerns why and how IGR institutions change. A broad research question such as this establishes an expansive universe of potential cases with which to study the problem. In this case, the universe includes all multi-level systems with IGR. Clearly, a narrowing down of choices is required. In Mill's method of difference, an effective qualitative comparison generally requires the cases to be most similar, such that a variety of independent variables that could affect the dependent variable are held constant. It also requires different values on the dependent variable to overcome the problem of selecting cases on the dependent variable (Geddes, 1990). Then one may examine which of the independent variable(s) are different in order to begin identifying the one that determines, or at least affects, the outcome.

As Lijphart (1971) points out, finding similar cases in the social sciences is possible so long as scholars avoid too exacting scientific standards, or what Sartori calls "over-conscious thinking." In this particular study of IGR institutional change, it is helpful to study multi-level systems that are closely matched on a broad list of independent variables, particularly the operation of their IGR system, their federal political structures as well as their basic economic structure. Over a period of time, there must also be change to their respective IGR systems that leads to a discernable difference on the dependent variable. Such requirements are demanding but a narrow paired comparison is appropriate to ensure the theory's robustness. The more dissimilar

the systems, the more independent variables that must be included, which waters down the analysis and its conclusions. History and experience provide two federal systems that meet all of these criteria: the Commonwealth of Australia and Canada.

Canada and Australia share many features that are relevant independent variables. Both are continent-sized countries with remarkable regional diversity. They are both former British colonies and therefore “share a common institutional architecture, combining the formal, constitutional distribution of power of federalism and the conventional concentration of power in the executive found in Westminster-style parliamentary governance” (Sayers & Banfield, 2013, p. 186). They also both have majoritarian electoral systems (see Lijphart, 1999). Both are multi-cultural, liberal-democratic societies that are endowed with an abundance of natural resources. Such abundance has been leveraged by both countries to create post-industrial, capital-intensive, free-trading economic unions with relatively high living standards. Their past economic histories include both resource-intensive and protectionist development.¹⁶ When examined according to the characteristics of their economic systems, both Canada and Australia are clustered within the Anglo-Saxon typology (Pryor, 2005). This typology “has its historical origins in Great Britain and is patterned after the classical liberal ideas of Adam Smith and the constitutional precepts of classical liberalism” (P. Gregory & Stuart, 2014, p. 211).

The nature of their economies, whether of the resource-intensive/protectionist or diversified/free-trading variety, mean that both countries are exposed to world market conditions. Such exposure requires adapting to changing conditions, which their political systems are responsible for managing. Their federal nature, characterized by divided sovereignty over the

¹⁶ See D. Brown (2002) for more on comparing Australia and Canada.

economic union, means that both orders of government play significant roles in managing the country's adaptation to globalization and liberalization. At times, governments must coordinate their efforts, which requires either intra- or inter-state federalism. Since intra-state federalism is no longer operational,¹⁷ it falls to the IGR system to facilitate coordination. The combination of Westminster parliamentarianism and federalism means that both are primed to have IGR systems characterized by executive federalism. We have thus arrived at a significant similarity between Canada and Australia, one that is critical to this inquiry: both countries rely on their IGR systems and the executive branch of government to manage their similarly-structured economic unions.

There are some significant differences, particularly their institutional trajectories (see Sayers & Banfield, 2013). The Australian federal constitution assigns specific powers to the Commonwealth government, leaving the states with residual powers. The basic principle of Australian federalism is concurrency, whereby both orders of government share policy responsibilities. Over time, the federal government has extended its power into many policy fields via its spending power, its paramountcy in areas of concurrency, and High Court decisions (Watts, 2008). At Canada's founding, both the federal and provincial governments were enumerated with exclusive powers in Sections 91 and 92 of the Constitution, respectively. It was believed at the time that the orders of government would operate independently within their spheres of power, with few policy areas being concurrent. This is the concept of dual federalism and is one of the major differences between the Canadian and Australian constitutions. In

¹⁷ See David Cameron and Simeon (2002) for the Canadian case and Bach (2003) for the Australian case.

Canada, mandatory cooperation is much less common than in Australia and the federal government is assigned residual powers.

Other significant differences between Canada and Australia are level of party system integration and vertical fiscal imbalance (VFI). Australian parties are more integrated across the orders of government and states are more reliant than provinces on transfers from the centre. Taken together, all these factors – the VFI, party system integration, and policy concurrency – propose that institutionalization should be likelier in Australia than in Canada. Special consideration is given to these alternative explanations.

Nevertheless, Canada and Australia had remarkably similar competitive styles of IGR for most of the post-WWII era. Each federal government made use of its spending power to expand its sphere of power and influence. Early efforts at intergovernmental cooperation in the 1960s gave way to acrimonious and heavily-conflicted relations between the orders of government. The result was the weak institutionalization of HoG summits in both cases (see Table 2).

In Canada, this culminated in the era of mega-constitutional politics, when Ottawa and the provinces twice attempted and twice failed to redraft the entire constitution. Despite this, cooperation in other forms does occur but it is ad hoc, compartmentalized, and under-institutionalized. According to the measures of routinization, FMCs are weakly institutionalized because they occur less and less regularly, promote limited contact between HoG, and are supported by a minimalist conference secretariat. Canada's competitive style of IGR is a result of the independence of both orders of government, a relatively more balanced fiscal federal system, and a parliamentary political system with its tendency for executives to dominate policy-making (see Chapter 5 for a full review of the Canadian IGR literature).

In Australia, its equalization system was described as fostering a “zero-sum game...[that] promotes political conflict and undermines the viability of reform” (Eccleston, Warren, & Woolley, 2013, p. 22). Yearly Premiers’ Conferences and Loan Councils were dominated by Canberra and promoted limited density of contacts between officials and produced financial arrangements with little input from the states. IGR was slightly more institutionalized than in Canada owing to the annual regularity of Premiers’ Conferences yet the outcome was similar to Canada’s in that the states and Commonwealth were often locked into bitter funding disputes. At times, attempts by the Commonwealth to manage fiscal transfers were thwarted by state administrations, which Canberra relies upon to deliver most services.

The comparison between Canada and Australia is valid having acknowledged their differences and similarities. Both countries exhibited relatively competitive IGR systems up until the 1990s, complete with weakly institutionalized HoG summits that were fractious, ineffective, and maligned in political discourse. Certain events, notably the dust-up at the 1990 Australian Premiers’ Conference – caused by cuts to state transfers – and the failure of Canadian FMCs to resolve the constitutional negotiations by 1992 provide good examples of the risk inherent in HoG meetings: failure is extremely counterproductive. Even the idea that meetings successfully produced agreements – for example, Canadian meetings’ ability to produce constitutional accords in 1987 and 1992 – must be weighed against the fact that the very method by which the agreements were reached, behind closed doors, is cited as the reason why they ultimately failed to be ratified (see Delacourt, 1993).

Then, a divergence occurs: Australia institutionalizes its HoG summit whilst Canada does not. Beginning in 1990, Canberra and the states launched a ‘new federalism’ initiative to avoid

policy duplication and reduce conflict between the orders of government (Galligan, 1995). Establishing productive and cooperative HoG meetings was seen as a way to overcome intergovernmental competition (Walsh, 2008). The cornerstone of the new initiative was a series of special premiers' conferences. Their main priority was to reform the economic union, including aspects of the federal system that were impacting the economy's efficiency and competitiveness.

Since that time, Australia has made extensive use of executive federalism. The special summits were formalized as the Council of Australian Governments. COAG meets twice per year and has concluded many agreements over the years. Instead of compartmentalized negotiations, Australia now has the institutional capacity to govern the entire IGR system and to prevent the acrimonious competition of the past (Carroll & Head, 2010). When placed up against the measures of routinization, Australia's HoG summit institutionalization is medium-strong. The SPC process initiated an increase in the density of contact between executives, including the establishment of negotiation taskforces. It maintained the regularity of meetings and created supporting institutions within the Commonwealth government. When COAG was officially announced, the supporting institutions were formalized and majority rule was allowed to function at times (states were able to refuse participation and let the rest proceed). Since its founding, the specificity of agreements has encompassed a broad range of policies, some of which were enshrined into law (Head, 2007). Currently, its level of routinization is between medium and strong because the chair and supporting institutions are under the purview of the Commonwealth rather than shared with the states (Wanna, 2007). In terms of value infusion, many interview sources both at the Commonwealth and state levels communicated COAG's

status as a vital institution of Australian governance; they actively sought to ensure its successful operation.

The use of executive federalism, the voluntary nature of the agreements and of governments' participation, and the mediation of government responsibility for policy areas are all characteristic of Brown's cooperative IGR typology. This is not to say that competition has been excised completely from Australian IGR. In response to the Commonwealth's reluctance to extend a state financing deal and to reduce its overall control of COAG's agenda, the Premiers established the Council of the Australian Federation (CAF) in 2006 in order to provide them with a permanent body to publicize their views and place pressure on the Commonwealth (Tiernan, 2008). Indeed, CAF could be considered a supporting institution of COAG, further strengthening its routinization. Therefore, competition remains an important though no longer dominant aspect of Australian IGR thanks to the institutionalization of its executive federal system. COAG is routinized and highly valued as a central policy-making institution of the Australian federation (see also Painter, 1998a).

In Canada, a similar reform effort designed to address the efficiency and competitiveness of the Canadian economy was re-launched with new vigour in 1993 under the auspices of the Agreement on Internal Trade (AIT)¹⁸ following several years of technical and low-level negotiations. Note that, in the early-1990s, both Canada and Australia witnessed the launching of microeconomic reform programmes. Rather than follow Australia into a new era of economic

¹⁸ The AIT is a trade agreement signed by all Canadian First Ministers that is designed to reduce and eliminate barriers to the free movement of persons, goods, services, and investment within Canada. It entered into force in 1995. Chapter 5 discusses the origin of the AIT's mandate and Chapter 6 follows the negotiations that led to its signing in July 1994.

reform and IGR system change, the Canadian effort stalled. On the economic front, the AIT languished for years as its policy-making process retaining the characteristics of competitive IGR. A new effort launched in the summer of 2014 by the previous Conservative government's Employment Minister Jason Kenney to restart the reform effort has been unsuccessful thus far.¹⁹ More recently, the new Liberal government has again tried to jump-start the process.²⁰

The convening of FMCs has decreased since the time of the AIT and in fact they have almost disappeared altogether. Papillon and Simeon (2004) regard FMCs as a once quasi-institutionalized body that is now just an informal mechanism. They believe it was quasi-institutionalized because, during the era of mega-constitutional politics, FMCs appeared to be held regularly and were focused on issues central to the *raison d'être* of Canada itself. FMCs were then de-emphasized after the constitutional implosion, with IGR becoming the "low profile, small steps approach of the Chrétien government to renewal of the federation, and a new focus on collaboration on specific programs through contacts at the official and ministerial level rather than first ministers" (Papillon & Simeon, 2004, p. 123).

The data on IGR meetings indicates that FMCs are not routinized nor are they infused with much value whereas meetings between department officials within specific policy areas, such as health care or finance, are considerably more institutionalized than FMCs (Simeon, 2006). Inwood et al. (2011, p. 43) report that 125 ministerial level meetings were held per year in the early 1990s, which fell to 70 in 1997-98 and then increased somewhat to 105 by 1999-2000.

¹⁹ See CBC News (2014).

²⁰ See Ivison (2016). At the 2016 CoF, Premiers announced an agreement-in-principle on a new Canadian Free Trade Agreement but its details and that of Ottawa's involvement are forthcoming (see Government of Ontario 2016).

Ministerial councils operated on top of the “more than a thousand federal-provincial-territorial committees and more than five hundred federal-provincial-territorial meetings each year” (ibid., p. 49). Contrast this to FMCs. After the era of mega-constitutional politics, FMCs were held infrequently, with just nine meetings convened in the 20 years since the Charlottetown referendum of 1992 compared to 29 meetings in the 20-year period leading up the referendum, most of which were held according to the 1985 Regina Accord that established the Annual Conferences of First Ministers (Canadian Intergovernmental Conference Secretariat, 2004). During PM Harper’s nine years in office, only one FMC was convened and he refused to attend CoF meetings despite receiving invitations from the Premiers. According to Papillon and Simeon (2004), the downplaying of FMCs took its toll as profound changes were occurring to the economy and to the role of governments. The Social Union Framework Agreement (SUFA), signed in 1999, was a rushed agreement that did not include Québec. Subsequent meetings on health care only produced minimal goals related to fiscal transfers rather than SUFA’s envisioned reorganization of the system (Forest, 2014).

There is no question that the value of FMCs plummeted after the failure to ratify the Charlottetown Accord, particularly since the continuation of the 1985 Regina Accord was contingent on its successful ratification. Efforts to restart FMCs shortly afterward also failed, leading to the dearth of activity today. When viewed against the measures of routinization, Canadian HoG summits are weakly institutionalized. The density of contacts amongst HoG has diminished and the regularity of FMCs is practically non-existent. It has no autonomous secretariat, especially since the Canadian Intergovernmental Conference Secretariat has “no ‘institutionally bounded’ configuration of actors which the secretariat could attempt to stand for

and whose interests it could actively pursue” (Bolleyer, 2009, p. 73). Canada too has seen an increase in the institutionalization of Premiers’ meetings through the Council of the Federation. However, their lack of connection to FMCs negates their contribution to the degree of routinization of FMCs. Unlike in Australia, FMCs fail to occupy the apex of the federation’s decision-making process, which leaves policy-making up to each order of government independently or within the lower levels of the IGR system. FMCs are disconnected from ministerial councils and so have proved incapable of driving the rest of the political system. Despite numerous attempts to institutionalize FMCs, they have faded away as an effective IGR decision-making institution. In fact, some even argue that economic adjustment is better served by not institutionalizing IGR at all (Haddow, 2012, p. 237).

Therefore, whilst Australia transformed its executive federal system to achieve COAG’s medium-strong degree of routinization and high value infusion, Canadian FMCs remain weakly routinized and not infused with much value. The task of the dissertation is to understand why two similarly-designed parliamentary federal systems diverged in this manner at the same time as they were developing programmes of microeconomic reform.

Theories of HoG Summit Institutionalization

What explains HoG summit institutionalization? Essentially, the question is asking what drives cooperation within IGR systems. When analyzing the literature, this broader frame of reference is helpful at identifying the variables that affect IGR systems – besides, specific studies on summit institutionalization are few and far between outside Western Europe.²¹ The following

²¹ See Murlon-Druol (2012).

review is not meant to encompass every possible explanation. Rather it highlights specific explanations for IGR institutional change that the literature has identified thus far. The prominent explanations are fiscal federalism, party system, and partisanship. Note that these alternatives are similar to the list of independent variables that differ between Canada and Australia.

Federations usually experience some sort of VFI, which is an asymmetry between revenues and spending responsibilities across the orders of government.²² Generally the problem manifests itself when the centre government's revenues exceed its responsibilities, leaving sub-units unable to fully finance their activities. Australia's relatively high VFI locks the states into a tight relationship with the Commonwealth. The fiscal federal system is managed via the Loan Council and Premiers' Conferences. The Loan Council monitors and coordinates government borrowing (Jay, 1977) whilst Premiers' Conferences decide on yearly transfers from Canberra to the states (this does not include other transfers that Canberra sends through the federal budget, which is a serious point of contention for the states). It is logical that, as the Commonwealth-state fiscal relationship evolved over time, it would impact institutionalization beyond the fiscal sector in order to allow HoG to manage the full extent of their interdependence. Conversely, Canada's lower VFI translates into a reduced incentive to reform IGR, which goes some way to explaining the observed outcome in Canada. The provinces that rely less on intergovernmental transfers do not seek a high level of institutionalization, at least where fiscal federalism is concerned. Indeed, Canada has no equivalent of official yearly meetings that decide on intergovernmental transfers nor is public borrowing handled by something as transparent and interdependent as a Loan Council (although Finance Ministers do meet annually).

²² See, for example, Dollery (2002).

Fiscal federalism as an explainer of the institutionalization of HoG summits holds some currency since summitry was required over time to establish and reform fiscal mechanisms and policies. Yet fiscal federalism has trouble explaining the timing of change. If fiscal arrangements were stable during the post-war era, then why did Australian IGR experience significant change in 1992? If the recession in 1990-91 instigated major fiscal changes, then why did past recessions not lead to institutional change? In Canada, the era of cooperative federalism – whereby provinces were fiscally dependent on federal transfers to establish the welfare state – did not succeed in institutionalizing summits. Rather, it was the constitutional negotiations that led to the 1985 Regina Accord, which was then followed by a period of summit de-institutionalization and which occurred sometime after the provinces attained greater fiscal independence. The point is to explain the timing of the change as well as the change itself.

Therefore, fiscal federalism may set the trajectory of IGR – towards more or less cooperation – but it seems little involved in progressing the system one way or the other. This raises an important question for the case studies: is a relatively high vertical fiscal imbalance responsible for starting an IGR system reform process? The answer may be that fiscal federalism helps actors to recognize the inherent problems of their IGR system but that other variables influence the actual outcome of reform, i.e. whether the level of institutionalization actually changes. These issues are interrelated and are examined specifically in the case studies.

Another set of hypotheses for IGR institutional change involves political parties. McKay (2001) views political parties as the primary vehicle for articulating regional interests/provincial distinctiveness. He follows the lead of Riker (1964), who contends that a federal system's overall level of centralization – and harmony (Riker & Schaps, 1957) – is determined by the party

system's level of centralization. Rodden (2006b) argues that reform of intergovernmental agreements in Canada and Australia was conditioned by electoral externalities that emerged from the party system. Reform occurred in Australia because the same political party held elected office in both orders of government, thus tying together state and federal electoral fortunes, which increased the incentive for states to make concessions on specific benefits in order to achieve broader national reforms. In Canada, a lack of party system integration results in heavy political competition between orders of government, producing an incentive to retain as many benefits as possible, which thwarts any effort at national reform. A lack of integration coupled with distinct provincial party politics makes unified government across Canada practically impossible.

Wibbels (2005) understands that the level of partisanship affects IGR, which Esselment (2012) confirmed in her study of Canadian IGR. Esselment argues that despite what is in the best interests of a province, partisan considerations do not affect the substance of an agreement. Rather, partisanship's impact is felt on the process of negotiation, i.e., on whether an agreement is actually reached and kept by parties that oppose each other. These findings confirm Filippov, Ordeshook, and Shvetsova (2004), who consider parties as key factors in the stability of federations.

In terms of IGR institutions then, these authors posit that political parties and party system determine change. This takes the form of like parties from both orders of government working together better than unlike parties. The level of integration of political parties also determines the level of cooperation or conflict in an IGR system. A HoG summit is more likely to be institutionalized when one party is in power across all or most of the orders of government

and even more likely if the party system is integrated. Australia's integrated party system should thus make institutionalization more likely, although the results of analyses on partisanship's effect on Australian IGR have been mixed (Sharman, 1994). In Canada, the party system is different in every province and little connected to federal parties (Filippov et al., 2004; Haddow, 2015; Pruysers, 2015), which may explain the difficulty of institutionalizing FMCs.

Riker's analysis suggests another way to consider institutionalization: what forces lead to centralization or decentralization in a federal system? Although increased cooperation does not necessarily equal increased centralization, the construction of an institutionalized meeting of all sovereign actors can be construed as a form of centralization, such that the sub-units are bound to each other and to the centre government more tightly. If the centre government controls the agenda and timing of meetings, then a regularized summit is at least a loose form of centralization. However, centralization is not institutionalization. Returning to the measures of routinization, strong institutionalization is better construed as a strengthening of the overall federal system rather than giving more control to the centre (hence why COAG is not yet strongly institutionalized). If the centre government did retain control, then, according to the measures of routinization, that meeting would be at a medium level of institutionalization: the secretariat would not be independent, majority rule would not be possible, and internal functional differentiation would be reliant on centre government-controlled ministerial councils.

Looking at partisanship slightly differently than above, Turgeon and Wallner (2013) conclude that political parties shape the level of centralization in Australia and Canada. They measure partisanship with taxing authority, concluding that Australia had a consistent supporter of centralization in the Labor Party hence Australia's more centralized taxation system whilst in

Canada support for the left-wing federally has been intermittent. Therefore, the provinces retained significant taxing authority. Again, institutionalization may be more likely in a more centralized system composed of less powerful sub-units.

Moving on from partisanship, Broschek (2011) looks at historical developments, such as critical junctures, that launched a polity onto one trajectory or another. According to this kind of analysis, instances such as conflicts, constitutional conventions, or court decisions heavily influence whether a federal polity is more or less centralized. Identifying specific critical junctures is a challenge for qualitative analyses. Nevertheless, it is useful to pinpoint moments in time when change occurs and to process trace the before and after. Generally, critical junctures have long gestation periods whereby they unfold over a space of time much longer than a single moment (see Pierson, 2004). Thus, the focus is less on the critical juncture itself and more on process tracing observed trends and the mechanisms of change.

The party system and partisanship variables are important elements that help to explain institutionalization. The reason why is because of executive federalism. In parliamentary system, executives – and the partisan political parties that occupy them – play a significant role in managing the IGR system. Various factors impact on actors' decision-making, including their partisanship and the party system. The main problem with these analyses is that they are unable to determine why change occurred at a specific point in time. This is because the party systems in both Canada and Australia have remained relatively stable for most of the post-war era. Therefore, if Australia's higher level of party system integration couple with unified party governance are responsible for economic and institutional reforms, then why did microeconomic reform or the founding of COAG not occur in 1965 or 1976, when the Liberals occupied most of

Australia's governments, instead of when Labor was in power in 1992, as Rodden notes?²³ Unified government also cannot explain certain reforms, such as to the Commonwealth Grants Commission, because the changes occurred during a change in federal governing party in 1973, as well as the establishment of the GST in 2000, when Liberal PM John Howard faced off against Labor governments in the three largest states. Clearly, the process tracing of change is required. Additionally, unified government in Australia is sometimes a misnomer since in-fighting within the Labour Party is a notorious part of Australian political history and because the Liberals have assumed power nationally only in coalition with the National Party. And in Canada, some reform is possible even with an un-integrated, competitive party system.²⁴ Considering the actor-centred nature of IGR, political parties and party system are important influencing factors yet their inability to fully explain the observed outcomes means that other variables are exercising some influence on actor behaviour.

Any comparison of Canada and Australia reveals a potential independent variable that is also a major difference between them: demography. Canada includes a significant minority of French-speaking Canadians concentrated in Québec, most of whom favour decentralization. Indeed, Erk (2008) concludes that heterogeneous federations tend towards decentralization. Since Australia has no geographically-concentrated linguistic minority of significant size, differences in demography are generally regarded as a significant factor in generating the outcomes observed in Canada.²⁵ Yet just because a difference exists does not mean it

²³ Australianpolitics.com (2015), "Federal, State & Territory Governments since 1930." A similar chart is an interactive display at the Museum of Australian Democracy.

²⁴ See Little (2008) and his analysis of the cooperative reform of the Canada Pension Plan.

²⁵ For example, "[t]he lower level of tension across the Australian federation in comparison with Canada reflects not only less diversity across the states, but the reinforcing character of successful intra-state and inter-state mechanisms" (Sayers & Banfield, 2013, p. 203)

automatically explains the divergence on the dependent variable. In fact, Canada's demography has been a constant throughout its history and so is unable to account for the changes that may happen at a given point in time. Explaining its effect requires a process tracing methodology to conclude whether or not demography had a significant impact on the DV, especially considering that some of the variables already identified do play a significant role in one case but not the other. In other words, is there another difference between Canada and Australia that contributed significantly to the observed outcomes in both cases?

One suggestion lies in studies of institutional change within federal systems that have focused on the political economy. In his study of processes of federating, Rector (2009) identifies explanations for an increase in cooperation. First, he divides key players into vulnerable and non-vulnerable actors. Actors' vulnerability is contingent on certain economic, social, or geographic conditions and therefore such actors may refuse to cooperate unless and until federal institutions are established. These institutions must concretely bind the non-vulnerable actors to the new federation and prevent them from using their strength to renegotiate the terms of federation in their favour sometime in the future. With appropriate institutions, the non-vulnerable actor invests heavily in federal institutions. For example, Victorian manufacturing was vulnerable to its reliance on the New South Wales (NSW) market and so Victoria (Vic) held out on joining a customs union until NSW agreed to federate, thereby giving Victoria some control over the external tariffs protecting its manufacturing industry.

Rector's analysis demonstrates the importance of considering the political economy in the formation of federations. The theory presented below and the case studies that follow demonstrate that the political economy became a significant difference between Canada and

Australia that impacted their respective IGR systems. Indeed, Rector's study is a launching point from which to continue analyzing the impact of the political economy on federal institutions. Once a federation is established, what role do vulnerable and non-vulnerable actors play in processes of institutional change? Does the political economy factor decrease in influence once a federation is established, thus allowing the other variables, such as party system, to take over? Regarding institutionalization, do certain actors refuse to cooperate until other actors commit to a higher level? Examining the role played by each actor helps to understand whether or not Rector's political economy explanation of cooperation continues to hold after federation and also to understand the factors that influence HoG summit institutionalization.

The Canadian literature has analyzed this issue to some extent. Scholars disagree on the extent to which liberalization, globalization, and economic integration have affected federal institutions. Some have concluded that "a substantial majority of the federations we have examined have adapted to global and regional integration change pressures without major transformations to their institutions" (Lazar et al., 2003, p. 1). They provide evidence that "other things being equal, external pressures will lead centralized federations to become even more centralized and vice versa" (ibid., p. 22). Are federations tightly bound to their original constitutional bargains?

Lazar et al.'s study examined change on a broad and major level whereas the dissertation examines specific changes to a very important institution. Changes to a HoG summit may not constitute what Lazar et al. refer to when discussing major transformations but it is change nonetheless. Other scholars take a bolder approach by suggesting that IGR systems are indeed impacted by outside forces, most notably Courchene (1995) and his concept of glocalization. He

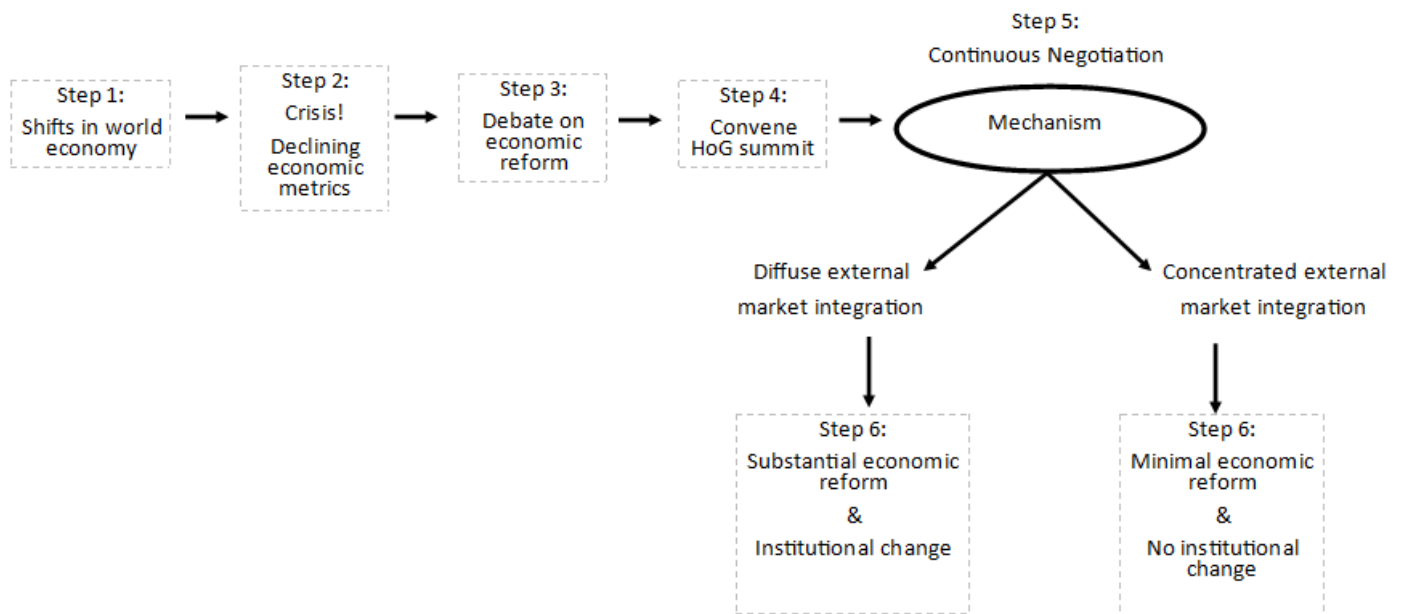
also contends that outside forces are causing irreparable change to Ontario's place in Confederation (Courchene & Telmer, 1998). The following political economy theory of HoG summit institutionalization also contends that IGR systems are impacted on by outside forces.

Political Economy Theory of HoG Summit Institutionalization

The following elucidates a theory for how the political economy – specifically internal and external trade patterns – affects the IGR system, and HoG summits in particular. The linkage between economics and political institutions is confirmed if changes in the global economy are reflected in changes to the IGR system. Therefore, the first step in the process of institutionalizing HoG summits is to consider shifts in the world economy (see Figure 1).

Whether it be new technology or a change in the prices of traded goods, shifts in the world economy have an impact on every economy, with the more open and trade-dependent economies experiencing a greater impact. Countries such as Australia and Canada – which are price-takers in the global economy – are particularly exposed to price changes. These shifts can occur gradually or suddenly but their result is usually the same: a sense of economic crisis pervades the country. Step 2 of the theory identifies this as declining economic measures.

Figure 1: Political Economy Theory of HoG Summit Institutionalization



A distinction must be made between a crisis and a shock. A shock is an immediate and sudden event, such as a one-day stock market movement or the release of unexpected economic news. A crisis occurs over a longer time period and may even be associated with a specific shock. Such a definition is important to the investigation because it implies the crisis has a gestation period: the time before a specific shock occurs during which the crisis has begun to manifest itself across various economic measures before reaching a crescendo. A recession may be construed as a crisis along with its accompanying unemployment, inflation or deflation, deficits, and fluctuating balance of payments. The recent crisis in the American financial and mortgage sectors caused enormous instability in capital markets around the world and severely affected employment. The 2015 oil shock is doing a number on energy-dependent economies. These crises do have specific shocks attached to them – such as the collapse of Lehman Brothers – but they are all part of overall trends that occurred over a longer period of time. Decision- and

opinion-makers may construe these trends as crises, cobbling together a series of specific shocks to define a crisis. Declining national competitiveness, falling productivity, and increasing inefficiency can all be regarded as ongoing crises, which must be acted upon in the face of global competition. A sense of urgency may develop among politicians, commentators, and business leaders, which commences a rush for solutions (Step 3). There may have been calls for reform in the past to deal with these problems but without the crisis context change was not forthcoming. The main point is that, for economic and institutional reform to proceed, a specific shock is not enough. Rather, a crisis context is required that not-so subtly hints at the need for a broadly-based reform programme, which is the basis for the mechanism of continuous negotiation between orders of government.

The reason why a crisis context is needed to engage the mechanism is because of the longer period of reform in multi-level systems. This is due to the fact that conflict is an inevitable byproduct of such systems. Conflict occurs in unitary systems of course but their more hierarchical decision-making process means that conflict is eventually resolved with orders from above. In federal systems, sovereign entities cannot solve conflict simply by taking or giving orders. They must negotiate on everything, including what the problem actually is before developing and deciding on solutions. All of this takes time; time enough for a series of shocks to develop into a crisis.

Significant conflict within federations is the result of a paradox. On the one hand, creating a federal state also means establishing an economic union with harmonized policies, open trade between sub-units, and overall integration. On the other hand, a federal state is created to endow sub-units with autonomy so they may provide their constituents with different policies

and choices (see Bakvis, Baier, & Brown, 2009; Oates, 1972, 1999). These choices at times may run with or counter to the needs of the economic union. Federalism thus presents a tradeoff that requires balancing the requirements of the economic union against policy autonomy and diversity. Searching for the right balance entails ongoing debate and discussion, and court decisions, all of which draws out the reform process.

If an economic crisis is theorized to impact IGR systems, then why did past crises not significantly impact the level of institutionalization of HoG summits? As discussed above, certain situations led HoG to meet in an ad hoc and informal manner shortly after the founding of their polities. Thus, in the past, crises have succeeded in increasing the level of institutionalization, albeit from a non-existent to a low level that then held constant and stable for most of the 20th century.²⁶

By the 1980s, the solution to a succession of economic crises, and to a general sense of malaise, was liberalization, which involved deregulation (or re-regulation), free(er) markets, open financial exchanges, floating currencies, and fewer regulatory burdens within internal markets. Liberalization was a substantially different solution to economic crises, to the point that it impacted on politics in a manner that other solutions had not. Wren (2006, p. 648) states that globalization “alters the calculus of political decision-making over economic policy”. Liberalization unleashed market forces that significantly changed the relationship between centre and sub-units in multi-level systems. It required governments to engage in more cooperative behaviour that included everything from simple information exchange to the joint

²⁶ This is in contrast to the European Union, which created its highly institutionalized European Council during its formative years rather than many decades after the EU was founded (see Imbrogno, forthcoming).

creation of policies. Such behaviour, including changes to decision-making institutions, was designed to cope with liberalization yet there remains the question of whether governments buy-in to a liberalization reform programme in the first place. In the end, most if not all developed countries have moved in this direction at various speeds.²⁷ Once liberalization is regarded as the cure to the economic crisis, the question then becomes how to enact reform?

In unitary systems, the answer is relatively simple: draft a bill and pass it through the legislature. But in multi-level systems, how does one engage a broadly-based economic reform programme that touches almost every aspect of policy when responsibility for policies is divided between jurisdictions? Depending on the policy, the question may be unnecessary since certain policies, particularly macro-economic ones, are held exclusively by one jurisdiction, usually the centre. Thus, for example, floating the currency or deregulating the banking industry can be accomplished via the centre's legislative process. But what about the internal market, where sub-units have the power to regulate, or concurrent areas of policy? The answer may very well be to convene a summit of HoG (Step 4).

The actual work involved in institutionalizing a HoG summit begins at a HoG summit, where it is recognized that solutions to the economic crisis will not be forthcoming without cooperation and collaboration between the centre and sub-units. History has shown that HoG summits are necessary at times to overcome one problem or another because HoG are the ultimate holders of power and sovereignty in their respective jurisdictions. They are also the focal point of central agencies, which coordinate and oversee government policies. Therefore, fixing

²⁷ See B. A. Simmons, Dobbin, and Garrett (2006). Indeed, Li (2015) operates on the premise that growth is partially dependent on export sophistication, which is an outcome of liberalization.

the economic malaise requires utilizing the IGR system, and not just any aspect of that system. Meetings between departmental bureaucrats and even between Ministers may be seen as being too technical, narrowly-focused, and fractious to handle the crisis and implement solutions. Negotiating across policy fields is key to the entire liberalization process because it requires more than technical-level negotiations; it requires the involvement of HoG to essentially “crack the whip”²⁸ and reach ‘package deals’, i.e. to make *political* choices between technical tradeoffs. Therefore, for the crisis at hand, the solution can only come from the top.

Now that a summit or series of summits is convened, the next step in the institutionalization process depends on what happens at them. Once convened, politicians want to be seen actively solving problems and making progress.²⁹ Since both orders of government are now in it together, their mutual incentive to succeed is high even though success is not guaranteed. They face a situation that requires negotiation over time to address, or at least attempt to address, all the various angles of the crisis. This process of continuous negotiation is the mechanism that propels institutionalization (Step 5).³⁰ More than once have negotiations at HoG summits stalled because of conflict or were abruptly called off because fundamental disagreements emerged. The key to understanding the institutionalization of HoG summits rests with the incentive to cooperate during continuous negotiations.

Continuous negotiations is the focus because economic issues are multifaceted: take competitiveness, for example. How do politicians in a multi-level system address falling

²⁸ This reference is from a *Financial Times* commentary on the EU-USA free trade negotiations: “The...risk is that ownership of the negotiations falls into the hands of the technocrats. Experts in, say, food hygiene or public procurement can always find reasons to disagree. The talks will succeed only if the politicians crack the whip” (Stephens, 2013).

²⁹ See Scharpf (1997), who regards actors’ interest in change as the main driver of institutional reform.

³⁰ It is related to the idea of contract-making, see Kimel (2007).

competitiveness? They will need to address whether industries are protected by tariffs, the structure of industries, and whether or not export subsidies are available. They will need to think about industrial relations and wage negotiations, transportation linkages, and regulations in such diverse areas as packaging and advertisement. How do firms find investment? Is a sufficient pool of skilled labour available? How much do firms and public education engage in research and development (R&D)? All of these in one way or another impact a polity's competitiveness on the international stage, which cannot be addressed by the natural competitive rhythm that forces firms to change and adapt. If politicians are not paying attention, if they are not adaptable to change, if they are confounded by internal conflicts, then the policies in place will become woefully inadequate. Indeed, the economic crisis may have emerged precisely because of the debate on the problem continued *ad nauseam* and delayed reforms hence why the crisis needs defining, why a HoG summit needs convening, and why negotiations become continuous: to get the ball rolling on this complex, multifaceted, multi-jurisdictional problem.

As leaders lock themselves into continuous negotiations to reform many if not all aspects of the economy, or in other words, as they manage the never-ending process of adapting to world market conditions, they come to recognize that their process of decision-making also needs to change in order to implement economic liberalization and manage the economy's adaptability. Informal networks of negotiating, which solved problems in the past, may now be inadequate to the task – they have become problem-creating, according to Helmke and Levitsky (2003, 2006). Leaders will call for more frequent meetings, a more formalized agenda, more research and preparation, for formal decision-making rules, and for the transformation of agreements into legislation. These are the same indicators of routinization, which is a key measure of

institutionalization. Eventually, actors may decide to perpetuate their decision-making process even after the initial reforms are concluded; institutionalization is a direct result of negotiating continuously. Continuous negotiation on economic policy is more specific than the fact that sovereignty in multi-level systems is contested; that the constitutional contract is incomplete and requires further negotiation (Rodden, 2006a). To overcome the generally contested nature of federal systems, each of the case studies focuses on a specific timeframe of continuous negotiation over economic policy.

However, this begs the question why political problems do not work to institutionalize HoG summits? The reason is found in historical experience. The HoG summits convened shortly after the founding of both Canada and Australia were primarily concerned with resolving political and fiscal issues. Once the issue was dealt with, subsequent summits were held but on different topics. The point is that these political issues did not engage a process of continuous negotiation within the IGR system, except perhaps at the lowest and more technical levels. In the case of Canada, resolving whether the federal or provincial governments controlled resources required many HoG summits but once the reorganization of power was agreed in a constitutional amendment, the next HoG summits were held on different issues.³¹ On the other hand, the need to continuously adjust in response to economic liberalization and internationalization requires constant negotiation and coordination. Economic reform and adjustment demand continuous negotiation, which is the mechanism that propels the emergence of a highly institutionalized process of decision-making that combines legislative rule-making with IGR decision-making, all

³¹ See Janigan (2012) for an account of these summits in Canada. Eggleston (1946) recounts a similar process regarding the transfer of unemployment insurance policy to Ottawa.

for the purposes of more effectively setting priorities and planning strategically for the polity's economic future.

And thus the process is complete: HoG summits are institutionalized due to continuous negotiations on a set of economic reforms that cross jurisdictional boundaries, thereby convincing leaders to reform their IGR system into a more formal and professional decision-making system. Rather, the process is far from automatic.

The study hinges on the incentive to institutionalize because continuous negotiation, as a form of contract-making, occurs “without necessarily a commitment by the parties to form...a relationship in future” (Kimel, 2007, p. 253). Federal systems have become marble cakes of various bargaining opportunities, which continuously alter the texture and flavour of the system. Thus, there remains the question of whether the emergence of the mechanism of continuous negotiation produces a bargaining environment that convinces leaders to commit to and lock themselves into a highly institutionalized system of decision-making, thereby adding a firm layer of icing on top of the marble cake. The need for continuous negotiation only points to what should be institutionalized: the HoG summit. It does not indicate whether or not these summit are in fact institutionalized into meetings. The actors involved are representing sovereign entities after all, with interests that do not always overlap: “actors have leeway in how they make use of opportunities offered” (Petersohn, Behnke, & Rhode, 2015, p. 627). It can also be argued that centre and sub-units have continuously negotiated over economic issues since their polity was founded via informal HoG summits, in front of the television cameras outside summits, and certainly during elections. In certain federal systems, conflict is managed competitively and summits are under-institutionalized whilst in others conflict is managed cooperatively with highly

institutionalized meetings.³² What are the incentives that drive leaders to accept radical changes to their IGR system during this time of perceived economic crisis? And where do these incentives originate?

Many incentives drive political leaders. The most important is re-election. The standard view emphasizes political incentive structures like political parties, legislative organization, and electoral rules, which were discussed more specifically above (Inwood et al., 2011; Rodden, 2006a). Politicians must operate within these structures to achieve their goal of re-election. Federalism scholarship has embraced the view that such outcomes are determined by the “interplay between incumbents’ incentives and the specific architecture of power in federations” (Beramendi, 2009, p. 765). At times, incentives structures may lead actors towards non-cooperative behaviour whilst other incentives may lead them to organize formal shared rule, i.e., to institutionalize decision-making. The main issue is that these incentives are acted upon by politicians when making electoral calculations. One example of a calculation is choosing whether or not to deal with the economic crisis. Another example is the manner in which they choose to deal with it. Politicians may agree to participate in an intergovernmental process of economic reform in order to address a crisis that is beyond their own government’s capabilities. A successful effort may then lead to re-election or at least rebuff opposition attacks on the government’s handling of the crisis.³³ Or they may decide that non-cooperative behaviour has its own electoral payoffs. They may even be ideologically opposed to the reforms and refuse to participate.

³² See D. Brown (2002) for a full typology of IGR systems.

³³ See Gélinau and Bélanger (2005).

The main problem with the election-incentive approach to HoG decision-making and institutionalization is that re-election is a constant in a politician's life. Since certain federal structures have existed since the polity's founding, there must exist other incentives that push leaders toward the calculation that institutionalization has benefits that outweigh the costs. The political economy is one source of incentives for actors, who then respond to the crisis in order to restore economic growth and prosperity as part of a strategy to seek re-election (Wren, 2006). As Mattli (1999) discusses, economic externalities explain the demand for integration, which is initiated by a fiscally dominant player. Institutionalization may follow the same dynamic: it is demanded by economic union requirements but is only successful once the dominant players 'buy in'.³⁴ How then do economic structures and conditions lead actors to lock themselves into a decision-making system with their jurisdictional peers?

The dissertation postulates that an incentive to cooperate is generated from concentrated market integration internally and/or diffuse market integration externally. According to D. Brown (2002, p. 44), diffuse external market integration means that "no one bilateral relationship is so important...that [one seeks] institutionalized integration through bilateral means." An economy trades with an abundance of partners such that no one partner overwhelmingly dominates. Concentrated external market integration is the opposite: one trade partner dominates international trade. Concentrated internal market integration refers to a tightly-bound economic union whereas diffuse internal market integration refers to a highly regionalized economic union with few linkages between regions.

³⁴ Petersohn et al. (2015, p. 627) refer to it as the "strategic power of interested actors".

In order for sub-unit actors to agree to constrain their powers – by constructing a formal IGR decision-making process – they must understand that their concentrated internal market integration is so great and irreversible that they must act collaboratively in order to maximize economic potentials. For institutionalization to occur, leaders of the major sub-units must ‘buy in’ to this narrative because their economic and political clout are vital to the success of the economic and institutional reform efforts. With the major sub-units in agreement, the other, smaller jurisdictions will follow suit and lock themselves into a decision-making structure with the more powerful centre and sub-unit governments in order to more effectively manage the reform process, enjoy its benefits, and prevent their being overrun. Therefore, a highly institutionalized HoG meeting is established when a broadly-based economic reform programme is engaged within a concentrated internal market context.³⁵ Petersohn et al. (2015) state that “party preferences and parties’ negotiation power interact with the negotiation mode, thus influencing [outcomes]”. HoG summit institutionalization occurs when incentives from the political economy impact actors’ behaviour during continuous negotiation on economic union reform.

The EU is the best example of this case (Krapohl & Fink, 2013; Moravcsik, 1998). Ensuring the health and growth of internal trade by maximizing efficiency translates into a political incentive to improve the policies that affect the internal market. Reforming these policies creates an incentive to improve and restructure the process of policy-making, hence the turn towards highly institutionalized HoG meetings (see Imbrogno, forthcoming).

³⁵ Diffuse internal trade will manifest itself as bilateral or intra-regional IGR rather than multilateral.

Rather than rely on concentrated internal market integration, sub-units may in fact trade more heavily with external partners. If the external market integration is diffuse, then sub-units may find that separately they are unable to maintain their competitive positions vis-à-vis their multiplicity of trade partners. The centre may also come to realize its inability to reform the national economy without the sub-units, which have different economic structures and policies. All jurisdictions, again the major sub-units in particular, will understand that improving competitiveness requires an efficient domestic market, investment in infrastructure, and reform of government services and government-regulated industries, such as telecoms. Thus, diffuse external market integration is evident from the common position that the polity and its sub-units have towards its trading partners. As Krapohl and Fink (2013) demonstrate, extra-regional economic gains may induce cooperation rather than competition if the dominant sub-units perceive that economic gains will be greater from cooperation than from going it alone. Together, the centre and sub-units depend on their mutual responsibility to manage the economic union as well as external trade relations and foreign investment. Because of this, they will have a greater chance of success working collaboratively rather than by piecemeal or through independent reform. Therefore, even without concentrated internal market integration, a polity may still develop a highly institutionalized HoG meeting (Step 6).

What happens when external market integration is concentrated? Since “internal competition for extra-regional investment and export flows is an obstacle to cooperation” (Krapohl & Fink, 2013), politicians will not lock themselves into a highly institutionalized system of decision-making. Concentrated external market integration means that jurisdictions do not rely on trade between them for significant amount of their economic growth. Instead, they rely

on one trading partner and will pursue policies that maximize their economic gains based on this trade even if those policies negatively impact the economic union. This occurs despite Mattli (1999) finding that industrialized economies will tend to cooperate with each other to garner the gains from growth in intra-regional trade. If such regional trade is actually concentrated external market integration, then it will limit internal cooperation. Even if the reform process requires continuous negotiation, concentrated external market integration reduces the need for a highly institutionalized system of IGR decision-making to the point that it may be unnecessary and inappropriate (Step 6). Actors may regard such a system as placing too great a constraint on their jurisdictional powers, including the ability to formulate policies best suited to their particular circumstances. And if sub-units are competing with one another for economic gain, then formal cooperation would most likely break down as the various actors time and again fail to formulate common positions that satisfy all of their opposing interests. Attempting to sustain an effort at institutionalizing IGR institutions may in fact exacerbate political tensions between competing jurisdictions. Better that a more flexible, ad hoc system be constructed and maintained, which can deal with national issues whilst allowing for policy differences.

With concentrated external market integration, a highly institutionalized HoG meeting is not possible nor desirable even in the presence of a broadly-based economic reform programme. According to Krapohl and Fink (2013, p. 4), when considering cooperation, “each member has to calculate its share of the collective gains from regional integration against potential distributive losses of privileges” from when it was more autonomous/less integrated. Therefore, when examining the levels of institutionalization of different multi-level polities, it is worth understanding their particular market integration structures since these structures have a

purportedly significant impact on the calculations of actors as they decide on what level of cooperation/integration is best suited for them.

The above has highlighted in general terms several possibilities for the creation of highly institutionalized HoG meetings. Have any of these occurred in the practical political world? The answer is yes. The next section identifies the cases and elucidates their market integration structures. The remaining chapters then explore each case in detail in order to understand if and how HoG summit institutionalization is impacted by the political economy.

Australian trade: exporting, and reforming, together

The independent variable that is purported to explain the variance of the dependent variable is the internal and external trade structures of each case. Australian trade exemplifies some level of concentrated internal market integration. Notably is the high degree of diffusion of its external market integration. Of most importance regarding the external data is the trend over time, which signifies an overwhelming diffusion. The following outlines first the internal data and then compares it to the external data.

Due to Australia's rather small population and its vast geographic area, it comes as no surprise that data on internal trade is difficult to compile. Inquiries to the Commonwealth and several state governments revealed that the Australian Bureau of Statistics (ABS) does not systematically collect this data, nor do the individual states. Indeed, Naqvi and Peter (1996) advocate for the collection of just such data. Quoting directly from the ABS Assistant Director for State Accounts:

Data on Interstate Trade has no direct data source and so is not directly measurable. Estimates are modelled at the level of Total Domestic Exports to all States, Total Domestic Imports from all States and Total International Trade

Exported to States. These estimates are included in the Balancing item of Gross State Product.³⁶

Since these figures are the best estimates available of internal trade, they are used with that caveat to compare to Canadian trade, which is actually measured by Statistics Canada.

The estimates from 1990 through to 2013 were graciously provided by the Assistant Director. Actual measured data from the ABS prior to 1990 is contained in sporadic reports on inter-state trade for the smaller Australian states. Both of these data sets are combined to calculate the total value of internal versus external trade relative to the economy as a whole and to determine the structure of Australia's external trade. A state by state approach is first employed before turning to the national figures for internal and external trade.

Between 1983 and 1989, Western Australia (WA) experienced some growth in its inter-state exports. In 1983, it exported A\$1.4 billion and by 1989 that figure was A\$1.8 billion, a growth rate of 26%. WA's inter-state imports far exceeded its exports, generating an internal trade deficit of A\$4.7 billion. In the same period, its foreign exports increased by 75%, which were comprised of resource-based manufactures, such as food and beverages and base metal products (Industry Commission, 1995).

To compare the relative sizes of WA's internal and external trade, its total value of trade (\$20 billion in 1989) was calculated by adding the value of internal and external imports to the value of internal and external exports. The value of WA's internal trade (both imports and exports) equalled 40% of its total trade value (Australian Bureau of Statistics, 1990a). In Queensland (QLD) in 1987, the proportion of its internal trade to the value of its total trade was

³⁶ Email exchange between author and ABS, 30 June 2014.

roughly similar, at 45%. QLD also had an internal trade deficit of A\$3.5 billion (Australian Bureau of Statistics, 1987). South Australia (SA) had neither an internal trade surplus nor deficit in 1988, with cars, car parts, and manufactured good making up the bulk of internal trade, most of which was destined to or received from Vic and NSW (Australian Bureau of Statistics, 1990b).

After 1990, internal trade expanded in line with the 20-year long boom in the Australian economy (see Figures 2a and 2b). The larger states of NSW and Vic experienced growth rates in exports of 64% and 104%, respectively, between 1990 and 2013 (with inflation factored out according to Reserve Bank of Australia calculations). Commodities certainly had an effect, with the resource-rich states of WA and QLD experiencing whopping growth rates of 424% and 252%, respectively. The same story is evident in internal imports. The value of NSW's imports grew by 70% between 1990 and 2013, Vic's grew by 76%, whilst WA and QLD again led the states in import growth, at 316% and 180%, respectively. In 1995, QLD's main inter-state imports were cars and car parts, iron and steel, clothing, and pharmaceuticals. Despite such rapid growth, the resource-rich economies remained in deficit with their neighbours (see Chart 2), with WA and QLD's internal trade deficits increasing by 486% and 173%, respectively. Victoria experienced dramatic growth in its surplus, by 464%, compared to NSW's more modest 153%. The larger states seem to be supplying their neighbours with the equipment and materials necessary to operate their resource-intensive economies, which then send most of their output abroad. Incredibly, SA was near deficit in the early 1990s before recording sustained internal trade surpluses, which experienced a whopping growth rate of 3,297% (it certainly pays to have a world-renowned wine industry!).

In the decade from 1982 to 1992, GDP growth was highly regionalized. Higher growth, based on the export of primary resources, was experienced in WA, QLD, and the NT, with WA the fastest growing state in the 1980s. These states also did not have intensive manufacturing, a sector that underwent considerable restructuring during the 1980s owing to the tariff reductions (Bureau of Industry Economics, 1994). Their commodity and foreign trade orientation facilitated higher growth during a decade of relative economic stagnation in the southern states. WA was the most export-oriented state, with 40% of its output destined overseas; QLD was second at 21% (Bureau of Industry Economics, 1994). Whilst the large internal trade deficits demonstrate that economic growth in the northern and western regions does benefit the south, in the end, economic growth in these areas is far more dependent on foreign trade than internal. And the boom in these regions was not enough to lift the economies of the manufacturing-intensive, lesser export-oriented states.

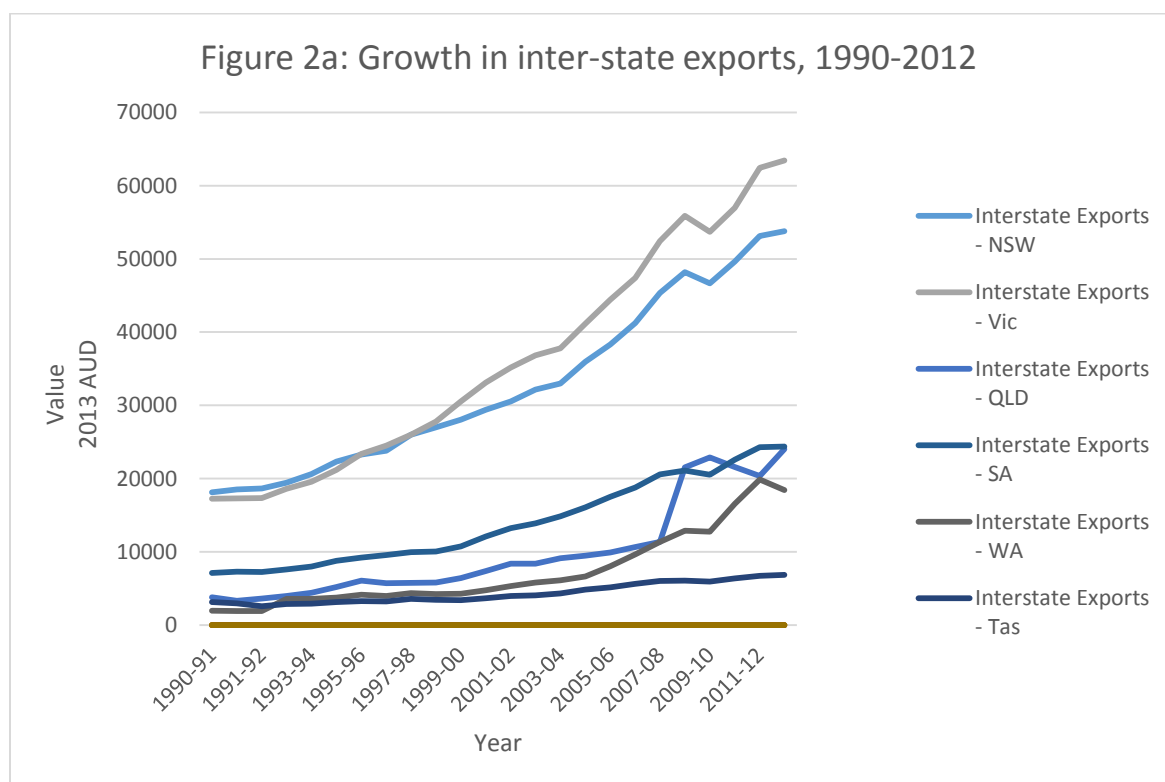


Figure 2b: Growth in inter-state imports, 1990-2012

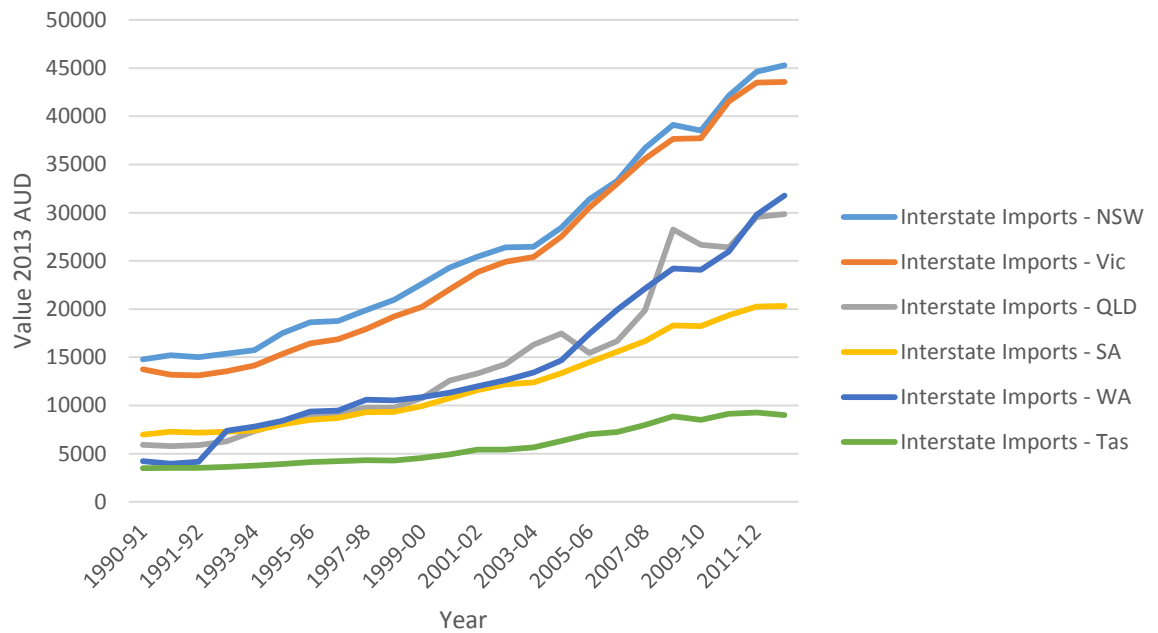
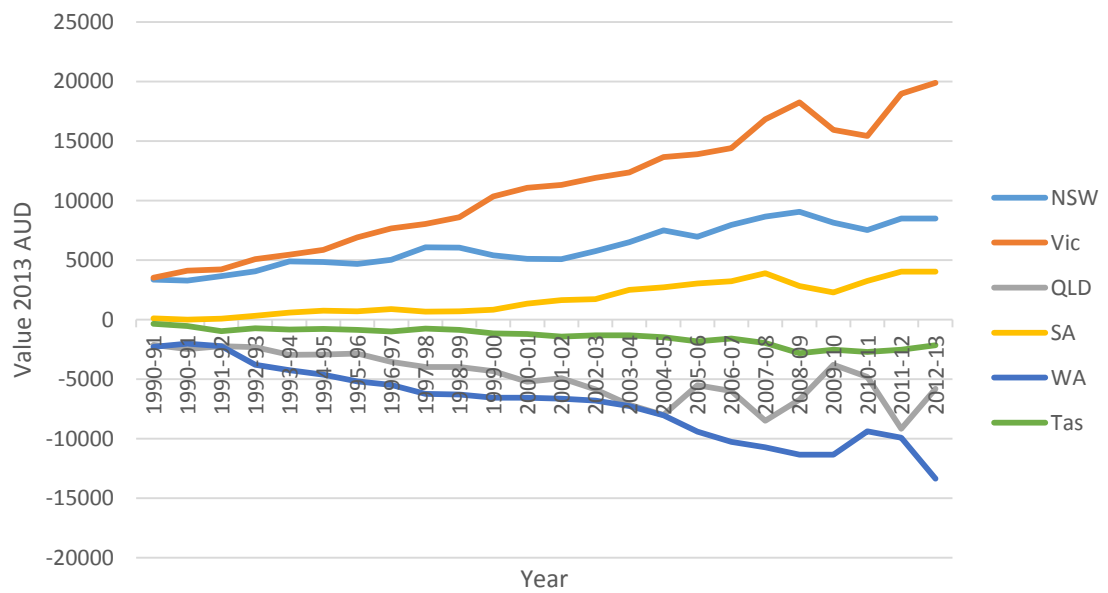


Figure 3: Inter-state trade balance, 1990-2012



The growing importance of international trade to the Australian economy is evidenced by its share of Australian GDP. In the early 1960s, its share of GDP was 34% and remained at 31% a decade later. By 1996, at 40%, a century-long trend of decline had been reversed yet it was still below the figure of 50% recorded in the mid-1800s (Snape, Gropp, & Luttrell, 1998, p. 9). Into the 1990s, foreign exports grew at a remarkable rate, measuring 11.3% growth as a percent of GDP in 1991, 9.5% in 1992, and 9.5% in 1994 (the average growth rate between 1990 and 1999 was 7.4%). Into the 2000s, the growth rate slowed to less than half of its levels in the 1990s (the average was 3.4%) (World Bank, 2015a).

These growth rates are impressive and reveal the sustained boom that the Australian economy experienced after the 1990-91 recession. It is somewhat surprising then that the Commonwealth chooses not to keep accurate figures on an economic sector that sharply reflects overall economic trends. Yet these growth rates are based on absolute values, which do not indicate their actual importance to the overall economy. Did the economic boom affect the composition of total trade?

One note on the data itself before proceeding with the comparison between the internal and external trade values. United Nations (UN) Comtrade data on exports is reported in USD for the year the trade occurred. The Australian internal trade estimates are reported in Australian dollars (AUD) under the heading “current prices value”, meaning that figures are in 2013 Australian dollars. To measure the relative size of Australian internal and external trade, the internal trade figures need to be converted into the same year and dollar value as the external trade figures. To adjust for inflation, the inflation calculator at the Australian Reserve Bank website was used. The Australian Reserve Bank also provides the monthly exchange rate for

AUD.³⁷ To find a yearly rate, an average of the monthly rates was calculated. The total value of Australian internal trade – the total value of each state’s exports – is then converted into USD.

There exists a potential problem with the data, in that an import into SA from another state may then be exported to the rest of the world. Therefore, simply adding internal trade values to external trade values to obtain a total value from which to compare their relative sizes may produce an inaccurate figure. It could lead to a margin of error since it over-estimates the total value of trade, since the external trade value may comprise the internal trade value plus the value-added trade before export. Fortunately, the problem is correctable because the ABS provides figures for inter-state exports separate from the figures for the inter-state movement of overseas trade, (i.e., trade that moves between states but whose final destination is overseas). Therefore, the internal trade figure is an estimate of the value of internal trade only. Since data to UN Comtrade is provided by the exporting country, it is reasonable to assume that the export value sent to the UN by the ABS is a figure that does not contain any inter-state trade values. The assumption is reasonable since the ABS itself separately calculates the portion of inter-state trade that is destined for overseas. Thus at this juncture, it is reasonable to assume that the data available comprises separate internal trade and export trade valuations, which can be added together to draw a picture of the trade structure of the Australian economy. The following analysis proceeds on these assumptions.

The results are consistent with ABS calculations from the 1980s. In 1990, Australian internal trade (the total value of all states’ exports) was valued at \$29.1 billion whilst total trade with the world was valued at \$36.1 billion. Based on these figures, Australian internal trade

³⁷ See <http://www.rba.gov.au/statistics/historical-data.html>.

represented 38.7% of the total value of all Australian trade in 1990. The proportion remained relatively steady, at 43.5% by 2005 (internal: \$77.8 billion; external: \$101.3 billion). Thus, both internal and external trade have experienced significant growth, with internal trade remaining in lockstep with external trade to maintain roughly the same proportion as in the 1980s. Therefore, the size of Australia's internal trade is large enough for concentrated market integration, especially considering the myriad of other linkages between states, such as education and sport.³⁸ It now remains to understand the composition of Australian external trade.

The structure of Australian external trade has changed dramatically over the course of the post-war era. In 1955, Australia was characterized by concentrated external market integration, with Europe and the UK receiving 63% of Australian exports (UK 36%, Europe 27%) whilst Japan imported 8% (EPAC, 1986b). By 1965, the UK was still on top, but its ever-closer relationship with Europe was beginning to have an impact, as was the boom in Japan. Australia's top five trading partners, measured as a share of the total value (in USD) of exports during that year, were the UK (18%), Japan (17%), EEC (15%), and USA (11%), with New Zealand (NZ) and China tied for fifth spot (6%) (see Figure 4). The shift to East Asia picked up markedly as the UK's entry into the EEC radically altered its trading relationship with Australia. By 1975, the UK was knocked from top spot to sixth (4%), with Japan occupying first place (30%), followed by the EEC (11%), USA (10%), ASEAN (8%), and NZ (5%).

Immediately evident is the growing dominance of Asian export destinations, with Japan significantly increasing its share of trade, along with the ASEAN countries (the same shift from

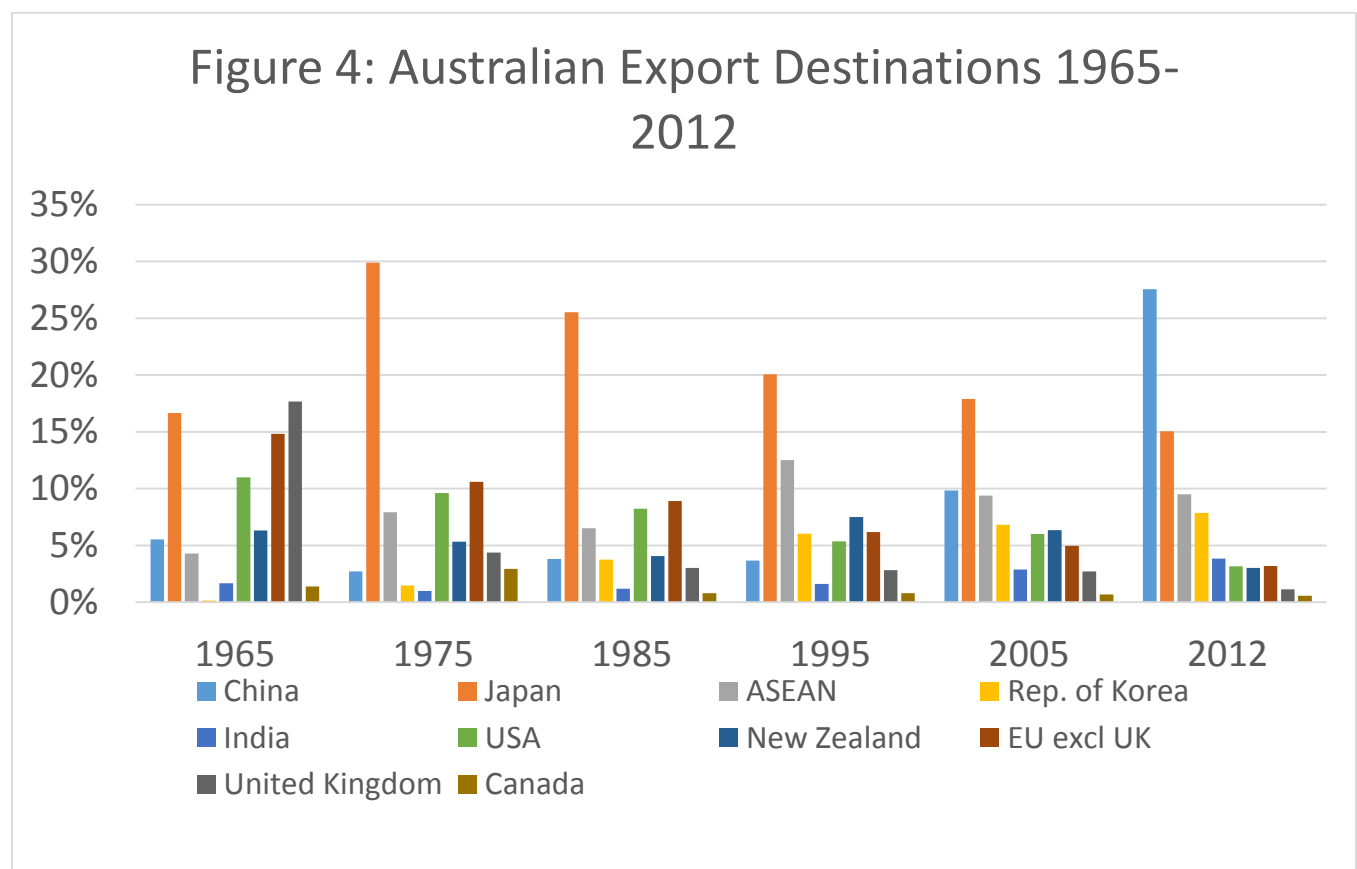
³⁸ See Helliwell (1998).

Europe/UK to Asia is also evident in imports).³⁹ Through to 1995, Japan continued to occupy top spot but its dominance had slipped (20%), whilst ASEAN trade continued to grow (13%), followed by NZ (8%), EEC (6%), South Korea (6%), USA (5%), and Hong Kong (4%). Therefore, between 1985 and 1995, the shift from concentrated to diffuse external market integration had begun. The Australian government calculated in 1996 that 80% of the increase in exports, including manufactures and services, was due to East Asia. Remarkably, NZ displaced the USA for third spot owing to the implementation of the Closer Economic Relations agreement, which included mutual recognition and some policy harmonization (NZ even participates in certain COAG meetings to maintain the agreement). Even so, on an absolute basis, the USA in 1996 was the largest source of imports and foreign investment and also was the principle destination of Australian overseas investment (Department of Foreign Affairs and Trade, 1996). However, the overall trend favoured continued growth from Asia. In 1995, exports comprised 17.9% of GDP, up slightly from 15.3% in 1985 (World Bank, 2015b).

The dominance of Asia was most definitely felt by 2005, with Japan (18%), China (10%), ASEAN (9%), and South Korea (7%) knocking Australia's western trading partners out of the top five completely (NZ and the USA were tied for fifth place at 6%). Just seven years later, China completely displaced Japan as Australia's top export destination (28%), with Japan continuing to slip (15%) and ASEAN (10%) and South Korean (8%) trade holding steady. Interestingly, by 2012, India appears on the top five list (4%), further displacing the West. In 2005, exports comprised 18.1% of GDP and 20.9% by 2014 (ibid.).

³⁹ see EPAC (1986b).

The above highlights the dramatic swing in Australia's foreign trade pattern from a concentrated Western market orientation to a diffused Asian market integration. Certainly the remarkable growth in Asia contributed to this change. The question is: did diffuse external market integration generate a cooperative incentive between Australian governments?



The dramatic changes in the orientation of Australian exports, the gulf in cultural understanding between Australian and most of Asia, Australia's dependence on the high price volatility of commodity exports, and the relative inefficiency and lagging productivity of its economy all contributed to an incentive to cooperate. Within a short period of time, the small Australian states were confronted with the huge sizes and remarkable growth rates of the Asian

economies as well as the diffusion of their external trade. The Australian case demonstrates that such exposure to a rapidly changing world market forced Australian politicians to reconsider their competitive mode of IGR and usher in a cooperative IGR institution.

The case study shows that the Australian states alone could not reform and compete sufficiently to reverse the falling competitiveness and productivity of their economies. Despite internal trade's importance, the Australian economy as a whole is too small to sustain significant growth in value and employment. The case study further reveals that the Commonwealth also realized that its macro-economic reforms would have limited success if they were not accompanied by reform at the state level. Thus both Commonwealth and state politicians realized that only by reforming together could they improve Australia's competitiveness. The vulnerability of the small Australian economy to world market trends and prices, its relative inefficiency and vast geography, a growing diffusion in trade patterns, and its unfamiliarity with Asian business practices all reinforced a cooperative incentive that went beyond the normal constitutional linkages and the size of its internal market. Each jurisdiction was dependent on the others to reform the whole of the economy in order to increase both exports and competitiveness. The diffusion and volatility of Australian's export pattern and the vulnerability of each state's economy vis-à-vis world markets opened a window of opportunity to change Australian federal practices. Australia simply could no longer afford the competitive system of IGR that had governed it previously. The end result was the founding of the Council of Australian Governments.

Canadian trade: faceoff between north-south & east-west

In general terms, Canadian external trade is the opposite of Australia's. Whilst both have relatively concentrated internal market integration and are heavily reliant on foreign trade, the composition of Canadian external trade is very concentrated. In short, trade with the USA dominates foreign trade and overshadows the internal market. The national figures are examined first followed by a province by province breakdown.

For Canadian trade destinations, the export story could not be simpler: the USA always occupies the top spot and overwhelming absorbs the great majority of Canadian exports (see Figure 5). Beginning in 1962 (source: UN Comtrade), the USA received 61% of Canadian exports, with the UK far behind at 14%. Over the course of the next five decades, Canada became ever more reliant on USA trade. By 2000, the USA received a whopping 87% of exports. Its position has declined somewhat since then. In 2010, it received 76% of exports, still an overwhelming majority yet indicative of a trend just emerging in the data: exports to China grew from a 1% share in 2000 to 3% in 2010 and to 4% in 2012 (China has received approximately 1% of Canadian exports since 1965). In 1985, exports comprised 27.7% of Canadian GDP, 36.2% in 1995 and 37% in 2005. By 2014, the figure stabilized at roughly 30% (World Bank, 2015b).

Internal trade is of a lesser value than international yet remains, as in Australia, of some significance. Thankfully, Statistics Canada collects internal trade data.⁴⁰ In 1981, Ontario's exports to the world and to the rest of Canada were roughly equal at \$40 billion (all figures in Canadian dollars unless otherwise stated) (Courchene & Telmer, 1998, p. 278). In 1988, Ontario's inter-

⁴⁰ At the November 1995 CMIT meeting, Ottawa "reached an understanding with [redacted] that will permit the [internal trade] statistics to continue to be produced, and on a more timely basis than previously." (Industry Canada FOI request [A-2014-00391_0001], "Strategy Note, CMIT November 1995," p.7).

provincial goods exports were worth \$37 billion (17% of the province's output) whilst exports of goods outside Canada were valued at \$67 billion, such that internal exports represented only 35% of all exports. Two way trade between Québec and Ontario was valued at \$30 billion. Inter-provincial trade produced a \$12.6 billion surplus for Ontario whilst Québec's inter-provincial trade surplus was valued at \$2.5 billion. The disparity in surpluses existed because Ontario was the destination for 28% of all goods exported from the other provinces, with Québec the second largest destination at 23%.⁴¹ By 1995, Ontario's international exports were roughly three times the size of its inter-provincial exports.

This trend continued throughout the next decade. In 1998, Ontario's inter-provincial exports of goods and services were \$72 billion, compared to \$186 billion for international trade (internal exports fell to just 28% of all exports). By 2008, its inter-provincial exports were valued at \$112.5 billion. Québec is Ontario's largest trading partner, with 40% (\$28 billion) of its inter-provincial exports destined for 'la belle province'. Québec's total inter-provincial trade was \$38 billion in 1998, with Ontario receiving 60% of Québec exports. By 2008, its inter-provincial exports were valued at \$60 billion.⁴² Indeed, ON-QC trade accounted for 30% of all inter-provincial trade, with Ontario the clear winner: Québec recorded a doubling of its trade deficit with Ontario between 1992 and 1998 to \$7 billion. Meanwhile, Québec's international exports were valued at over \$69 billion, double the value recorded in 1992. Internal trade accounts for 36% of Québec's exports, making it significantly more reliant on the Canadian internal market than its sister province (Statistics Canada, 2000).

⁴¹ Archives of Ontario, Folder B705175 – Consultations with Private Sector, "Meeting with Mayors of GTA, Speaking Notes," 18 June 1993, p.1.

⁴² Statistics Canada (2008), CANSIM table 384-0002, "Interprovincial trade, by province and territory."

Turning to international exports, Canada's international export growth as a percent of GDP between 1990 and 1999 averaged 8.6%; between 2000 and 2009 it averaged -0.23%. In the last five years, foreign export growth has recovered somewhat, recording an average of 4.3% (World Bank, 2015a). Compared to Australia, the lost decade of the 2000s indicates that all of one's export eggs going into one overseas basket is a significant issue.

Nevertheless, for the provinces, the USA matters. Between 1992 and 1998, Ontario's international exports grew at an average of 13.2% a year to comprise 72% of total exports. This contrasts to inter-provincial exports, which grew at an average of 4.9% (Statistics Canada, 2000). The USA is Ontario's largest export destination, with 79.9% (\$151.7 billion) of Ontario's exports in 2013 headed south, compared to 82.6% in 2008. In 2012, 27.7% of Ontario GDP was derived from exports (Gauthier, 2014). According to Courchene and Telmer (1998, p. 278), if the disparity between internal and external trade growth continues, then "the pressures to focus all energies north-south will be overwhelming," which fuels their contention that Ontario is transitioning from heartland province to North American region state.

Québec too is reliant on international trade, which grew at 13.3% a year on average between 1992 and 1998 whereas growth in inter-provincial trade averaged just 3.6% (Statistics Canada, 2000). The result is that between 1990 and 1997, the destination of Québec exports shifted from 47% international and 53% inter-provincial to 64% international and 36% inter-provincial. International exports generated 58.6% of the employment that is tied to exports, with inter-provincial generating 41.4%. Over the same period, employment growth in international exports was 5.3% a year on average. Inter-provincial export employment actually declined, by an average of 3.4% a year (Institute de la statistique du Québec, 1999). In 2012, 68.5% (\$43.5 billion)

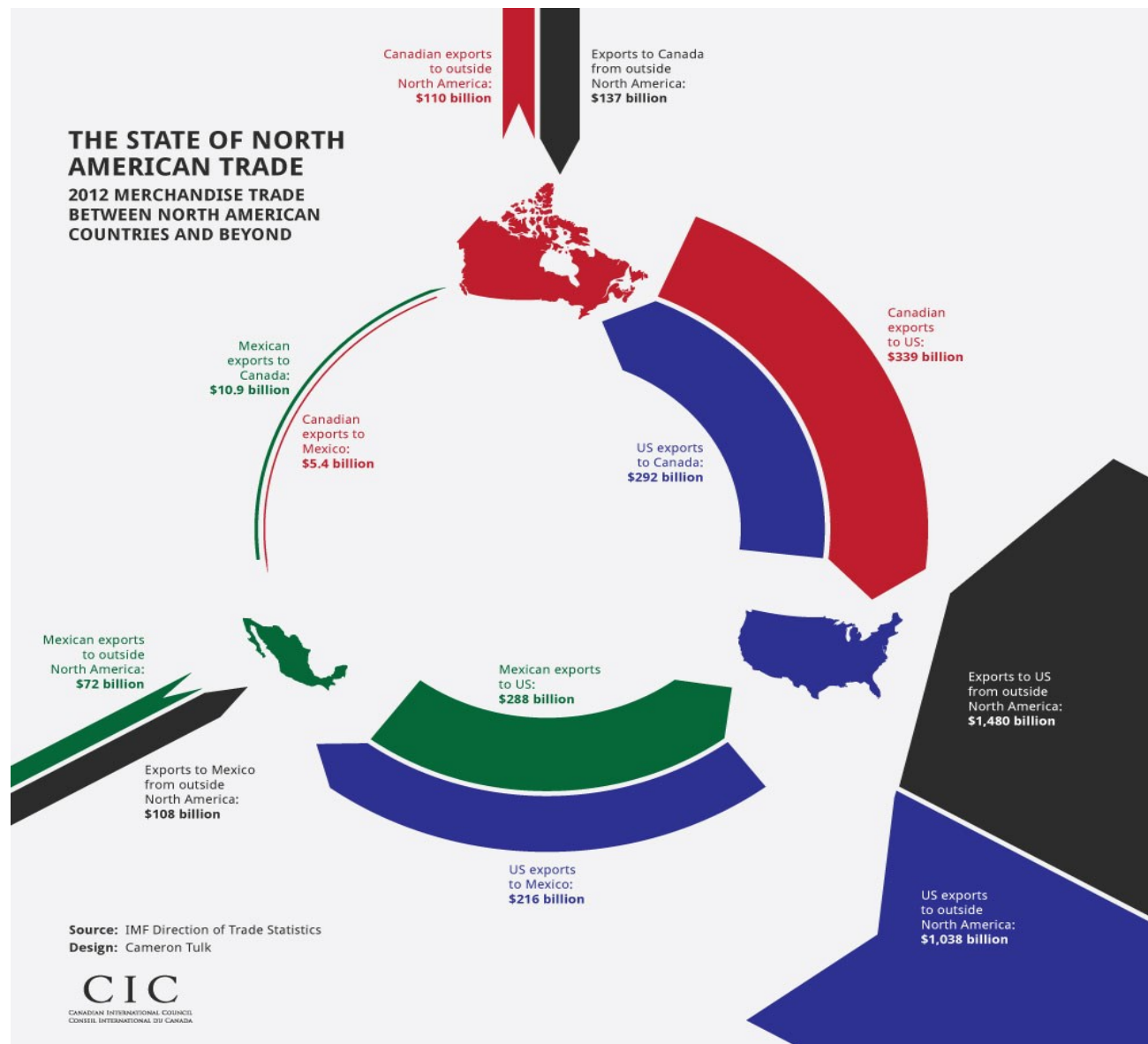
of Québec's exports were destined for the USA, down from 74.6% in 2007. In 2012, the value of merchandise exports was 17.8% of Québec's GDP (Tremblay, 2013). Clearly, it is international, specifically USA, trade on which Ontario and Québec are focused.

The story for the other provinces is broadly similar, reflecting a reliance on international/USA trade rather than inter-provincial. By 1994, only PEI exported more to the rest of Canada than to the world. As well, all provinces except British Columbia (BC) trade overwhelmingly with the USA. Topping the list is New Brunswick (NB), which sent 90% of its foreign exports to the USA in 2013, followed closely by Alberta at 88%. Ontario, Nova Scotia (NS), and Québec all sent roughly three-quarters of their foreign exports south. Only BC stands out as the least reliant on USA trade, sending 45.7% of foreign exports south. Unsurprisingly, it is also the province that relies most on trade with a variety of other partners, sending 38.9% of foreign exports to China, Japan, South Korean, and Taiwan (Library of Parliament, 2014). This trend has only grown over time. In 1994, BC sent 54.1% of its foreign exports to the USA, 24.8% to Japan, followed by 3.2% to South Korea (Howlett & Brownsey, 1996, p. 25).

In terms of relative balance between inter-provincial and international trade, Manitoba (MB) and New Brunswick are unique since they both recorded an equal weighting in their export mix in 1998, most likely reflective of their central location between major Canadian markets. All other provinces saw a distribution of exports in favour of international destinations, although Alberta and Nova Scotia only slightly so with inter-provincial exports comprising 42% and 44% of total exports, respectively. BC most closely resembles Ontario in that it is the second least reliant on the Canadian domestic market, although as mentioned BC's international mix is different.

Finally, all provinces experienced more rapid growth in international exports than in inter-provincial.

Figure 5: North American trade, 2012⁴³



⁴³ See OpenCanada.org, Canadian International Council. Accessed 12 October 2015 from: <http://opencanada.org/features/the-think-tank/graphics/how-integrated-is-the-north-america-economy/>.

A caveat remains to be analyzed with regard to the above figures. Calculations by Helliwell (1998, 1999) show that the density of trade flows between Canadian provinces is 20 times greater than trade between provinces and US states of roughly equal geographic distance and size, which holds or is greater across all sectors of the economy. Only the car industry between Ontario and Michigan lacked a border effect, a product of over 20 years of integration via the Auto Pact. The 1987 Free Trade Agreement between Canada and the USA (FTA) lowered the border effect from 20 to 17, a still significant gap between inter-provincial and intra-North American trade (Helliwell, 1999, p. 97). Through to 1996, the border effect settled at 12 whilst the density of linkages in services remained at between 30 and 40 (Helliwell, 1998, p. 115). Helliwell suggests that the reasons why national density is so high is because of trust networks and familiarity: “the global market is very much the exception, and the national market the rule” (Helliwell, 1999, p. 97).

This analysis suggests that internal trade in both Australia and Canada outweighs the importance of international trade. Helliwell employs a gravity model to measure the border effects of inter-provincial trade compared to trade between provinces and states. The premise is that the costs of distance matter. Closer markets will trade more with each other than they will with increasingly distant markets *regardless of borders*. For example, Ontario should trade the same amount with BC and American states of similar size and distance. Helliwell’s findings indicate otherwise. Therefore, other variables matter more than distance and its costs.

However, even though the density of internal linkages may be higher, the point is that the value and growth of international trade is higher than internal trade, and the gap between them is increasing. Helliwell (1998, p. 21) found that Ontario’s exports to California grew by 85% between 1990 and 1995 whilst those to BC and Washington shrank by 10% each, thus reducing

the border effect favouring internal trade. Therefore, the national economy relies increasingly on the world economy and therefore international trade garners the most attention from businesses and policy-makers. The impact is even more evident in Canada since its GDP is comprised of a higher share of exports than Australia's. The point is that Helliwell's internal linkages are important but they can also be taken for granted, allowing the focus to turn to international trade at the cost of the national economy and institutions. If Helliwell's density figures matter, in that they affect IGR as one might expect, then why is intergovernmental cooperation so weakly institutionalized?

With so heavy a reliance on USA trade, and with international trade the source of growth, the result is less cooperative Canadian IGR. The Canadian case study demonstrates that even when the mechanism of continuous negotiation is engaged – in this case during the AIT negotiations – it is incapable of single-handedly overcoming Canada's regionalized political economy in order to institutionalize summitry. Provincial economies are generally not focused on their east-west neighbours as they pursue regional development. Rather they are concentrated on their external positions. With relatively little incentive to coordinate economically, provincial actors are not prepared to lock themselves into a highly institutionalized decision-making structure with their economic competitors. Despite the potential gains from increasing the total competitiveness and efficiency of the Canadian economy – not to mention the gains from IGR reform – the dominant characteristic of intergovernmental policy-making remains competitive rather than cooperative. The latter does occur at the technical and bureaucratic level but does not filter up to the highest political offices nor involves the most

contentious policies. IGR is therefore a reflection of economic structures. The following chapters elucidate this in greater detail.

PART TWO:

THE COUNCIL OF AUSTRALIAN GOVERNMENTS

Chapter 3:

The Lucky Country and Microeconomic Reform

*We need the habit of adaptation – because the lesson of international competitiveness must be constantly learned and re-learned.*⁴⁴

Robert James Lee (Bob) Hawke
Prime Minister of Australia, 1983-1991

⁴⁴ Hawke (1991).

Why did Australian governments, comprising the Commonwealth, states and territories,⁴⁵ create and institutionalize their HoG meeting, known as the Council of Australian Governments (COAG)? South Australia (SA) Premier John Bannon (1992) gave an answer to this question in a 1992 speech at the ANU's Federalism Research Centre: "A unique political opportunity for major reform was presented" upon PM Bob Hawke's third re-election in 1990. The factors that led to this were: 1) the centenary of federation; 2) Hawke's search for a legacy; 3) five state Labor governments to balance the federal Labor Party's tendency towards centralization; 4) the resignation of Queensland's (QLD) long-serving premier and National Party leader, Joh Bjelke-Petersen; 5) New South Wales (NSW) Premier Nick Greiner's reform agenda; 6) premiers impatient with the federal system's inadequacies; 7) fiscal austerity; and 8) an 18-month period with no state or federal elections.

Bannon's⁴⁶ list contains the major political events of the time as well as party and institutional variables. It does not tell us which of the factors that established COAG were the most important and influential nor does it tell us how they impacted on and interacted with each other. Some factors emerged from the states and others from the Commonwealth, which behooves us to ask which order of government was more important to the founding of COAG? Also, no international factors are listed. Since Australia does not operate in a vacuum, more information is required. Finally, some of the factors are unique to Australia, such as its centenary and the individuals involved, whilst others are more generalizable. Is it at all possible to generalize the Australian case to other multi-level systems?

⁴⁵ Herein, when referring to the states, the inclusion of the territories (NT and ACT) is implied.

⁴⁶ John Bannon passed away on 13 December 2015. He "is remembered as a man of principle and a politician without ego" for modernizing the Labor Party and South Australia (Donnellan & Sexton, 2015).

Australian federalism is characterized by what Painter (1998b) refers to as 'arm's length' federalism, which refers to the Commonwealth's ability to set policy priorities for the states by virtue of its spending power. It is arm's length because Canberra has few tools with which to control the states' administrative activities once the money is transferred. Others have characterized Australian federalism as 'concurrent' federalism since most of the Commonwealth's constitutional powers are shared with the states (Galligan, 1997). An effect of concurrency is the oscillation throughout Australian history of periods of cooperation and conflict (Hollander & Patapan, 2007). Concurrency is emphasized in Australian politics because of High Court decisions and because the constitution assumes that Commonwealth and state powers are exercised concurrently (M. Keating & Wanna, 2000).

Galligan (1995) interprets COAG's founding as evidence of another period in Australian history of intergovernmental cooperation. Specifically, he reckons that certain procedures regarding Australia's finances were broadened to include other policy areas, which required a new IGR institution (M. Edwards & Henderson, 1995). Yet if Australia had elements of cooperation in the past, then why was a peak intergovernmental decision-making body not institutionalized some time before 1992?

In response, Painter (1998a) sees COAG as an innovation and not merely a continuation of past periods of cooperation. His study of 'collaborative' federalism provides an outline of the events leading up to COAG and produces a list of factors that parallels Bannon's list. But Painter does not provide, nor is it his intention to provide, a full accounting of the reasons why certain actions were taken; we are still left with an incomplete answer to the question. Painter (1995a) alludes to the fact that the Commonwealth needed the states for the sake of its microeconomic

reform program (there were questions concerning the limits of the Commonwealth's constitutional powers in pursuing the reforms). Painter concludes that COAG was established despite huge differences in the way federalism was viewed by the Commonwealth and states. The former, according to Painter, wanted harmonization and national standards whilst the latter were keen to reject Canberra's implicit managerialism and end its interference in their areas of jurisdiction. On the surface, these do not seem like sufficient reasons to create and sustain the most important institution of the Australian IGR system.

The following explains the reason why leaders managed to bridge their differences and agree to work together to both reform the economy and Australian IGR. Hawke especially thought 'outside the box' – the Commonwealth one that is. Rather than succumbing to another period of competitive federalism (Galligan, 1995), a moment of cooperation was fomented and institutionalized. Whilst Painter's work is invaluable for its detailed analysis of this innovation, it is insufficient at providing students of other multi-level systems with concrete lessons on the institutionalization of cooperative federalism in the form of a HoG summit. Finding a complete and satisfactory answer that connects all the different explanations and pronounces on their overall impact and importance is a compelling reason to continue investigating. An even better reason is to see if the Australian case offers lessons to other multi-level systems on the institutionalization of HoG summits. The results reveal the dynamics and interaction between all the various factors, which helps to understand if uniquely Australian or more generalizable factors are responsible for HoG summit institutionalization.

Using process tracing, this chapter and the next produce a more comprehensive answer than previous studies on the topic of COAG's founding. Together, both chapters examine

Australian politics at the time and seek to place all the factors into a coherent framework of analysis. At times this requires delving deep into Australian history and politics to fully understand how and why the factors that institutionalized COAG emerged and then coalesced in the early-1990s. It adds the external global environment to Bannon's list of reasons because it is an important generator of political incentives given Australia's relatively small size and open economy. It also highlights the value of leadership. In sum, Australia's changing place in the global economy steered its leaders toward an economic reform effort that eventually included reforming its system of intergovernmental decision-making, which culminated in the establishment of COAG.

The analysis proceeds as follows: this first chapter on Australia identifies the moment when COAG's predecessor, the Special Premiers' Conference (SPC), was proposed and outlines their *raison d'être*. It then goes back in time to identify why the proposal emerged and the factors that led to its implementation. The next chapter continues the story from when the SPC proposal is publicized and traces the subsequent events in order to understand how and why COAG was founded.

The first official COAG meeting occurred on 7 December 1992 in Perth, WA. It was preceded by a number of SPCs that were convened by PM Hawke. Eventually the SPCs themselves were recognized as having value and were formalized and institutionalized promptly thereafter. So where precisely did COAG come from? It is useful to begin each of the chapters on the Australian case by examining a speech delivered at the National Press Club (NPC).⁴⁷ The lead

⁴⁷ A former Governor-General described the NPC as "the great national arena to which the eminent and newsworthy are invited to perform" (Stephen, 1989).

off for this chapter was delivered by Bob Hawke on 19 July 1990. The next chapter begins with a speech delivered by NSW Premier Nick Greiner a few days later.

A 'Closer Partnership'

Dubbed the 'Towards a Closer Partnership' speech, Hawke announced at the NPC that "the time has come to form a closer partnership between our three levels of government".⁴⁸ Hawke made clear that the Commonwealth was not prescribing solutions, it was not "specifying outcomes" but instead was seeking "a process through which change can be achieved".⁴⁹ What kind of change did Hawke want and why was a 'closer partnership' the way to get it?

It is necessary to unpack the importance of Hawke's simple statement on the need for a process for change. Several sources indicate that the Commonwealth's desire to truly and fairly negotiate the issues was a major factor in the overall success of the SPC process, which ultimately led to the foundation of COAG. In Premiers' Conferences prior to 1990, the Commonwealth's stance towards the states was overbearing and dominant, to the point that there was very little actual negotiation. The Commonwealth's dominance had the effect of institutionalizing conflict (Walsh, 1992). From the states' point of view, the Commonwealth was presenting a 'take it or leave it' position. There are several anecdotes to support this assertion.

In a speech at the NPC, WA Premier Carmen Lawrence recalled a Premiers' Conference whereby the PM, acting as chair, called a vote that registered 6 ayes and 1 no, the Commonwealth having voted against, and declared that 'the nos have it'. Such a display of

⁴⁸ National Library of Australia (herein NLA), Speech by Bob Hawke at the National Press Club, "Towards a Closer Partnership," 19 July 1990 (see also <http://pmtranscripts.dpmc.gov.au/release/transcript-8059>).

⁴⁹ NLA, Hawke at NPC, 19 July 1990.

Commonwealth dominance affronted the states. She also mentioned that the Commonwealth frequently sets the priorities and “bludgeons” the states into submission. To be fair, she also indicated that the states do not always “offer the hand of cooperation”.⁵⁰ Yet she declared that “if the obvious failing of Premiers’ Conferences have lamed our federal system, than abolishing the forum would only serve to cripple it completely”.⁵¹ John Cain (1995, p. 157), Premier of Victoria, described Premiers’ Conferences as “a combination of ritual farce and bullying....closer to horse-stealing than horse-trading. A heavily centralist Treasurer ensured the trend was all one way”. HoG needed to find a way to work together since they had clearly failed to do so in the recent past, as the next example also demonstrates.

In the lead up to a typical Premiers’ Conference, particularly throughout the 1980s, state governments would be kept in the dark about the Commonwealth’s position, specifically its funding formula. Premiers would arrive in Canberra and conduct bilateral discussions with the PM to plead their own special cases. Yet Cain (1995, p. 158) wrote that “pre-conference discussions seemed not to matter,” a process that “created ill will and resentment”, and became increasingly fractious and ad hoc to the point that, at the 1990 Premiers’ Conference, the level of frustration boiled over. It is a significant critical juncture. Things were so bad, Hawke walked out of the conference and the states were in near revolt over the way in which they had been treated and the deal that was foisted on them. When the Hawke government began seeking even more changes to the economy and social life of Australians, a different way of negotiating was

⁵⁰ NLA, Speech by Cameron Lawrence at the National Press Club, 27 June 1990, nla.obj-222569106. An interview with a former senior state government official (19 June 2014) confirmed there was lots of acrimony at Premiers’ Conferences, sometimes between Premiers from the same party.

⁵¹ NLA, Lawrence at NPC, June 1990.

clearly required. Proposing 'a closer partnership' with the states to deal with the Commonwealth's reform programme meant a further round of Premiers' Conferences. The following addresses the reasons why summitry was turned to again even though it had failed so spectacularly.

Hawke's statement that the outcomes of the SPC process were as yet undecided was a clear signal to the states that the Commonwealth wanted change. Not simply a change to regulations or policies but a change in the overall tenor of IGR. Hawke sought equal partners at the negotiating table and wanted "sensible, practicable steps to get better cooperation within the framework of the Federal Constitution". Hawke wanted "a process which will produce results".⁵² The Ministerial Councils, which brought together ministers responsible for the same portfolio across the orders of government, were too decentralized and relied on informality to the point that they were inadequate for the task at hand. According to the former Chief of Staff of both the Victorian and NSW Premiers, Ken Baxter, "the degree of progressive, forward looking policy in these areas was minuscule...The torpor was reinforced by the system of Ministerial Councils, [which] should be abolished" (Baxter, 2008). Minuscule was not going to work for Hawke: "the challenge is broader and more urgent".⁵³ It was a challenge so great he made another, larger offer to the states in order to entice them to join the SPC process: he offered a review of Commonwealth-State financial arrangements.

The states with reform-minded Premiers, particularly SA's Bannon, NSW's Greiner, and Wayne Goss of QLD, were ready to meet the Commonwealth. In fact they had been ready for

⁵² NLA, Hawke at NPC, 19 July 1990.

⁵³ Ibid.

some time. Just prior to the 1990 Premiers' Conference, Bannon released an eleven point plan on financial arrangements and microeconomic reform. It was becoming apparent that financial arrangements were inadequate. Increasingly, state budgets were relying on transfers from the Commonwealth, transfers which made policy planning and financial forecasting difficult. As well, state budgets had to wait until the Commonwealth delivered its budget, which would contain spending priorities not included in the financial package discussed at that year's Premiers' Conference. Bannon's points were aimed at attaining certainty in the level of payments to assist with planning on a three-year basis and ensuring the full funding of Commonwealth policies that contained any state expenditure implications.⁵⁴ As well, the Commonwealth's tied grants were problematic, since states received funding for programs whose objectives and structures were not designed locally but by the Commonwealth, sometimes even in areas outside its constitutional powers.

This situation was a result of Australia having one of the largest vertical fiscal imbalances among the world's federations. By 1991, the Commonwealth was collecting 80% of taxes but it required only 50% to fund its operations.⁵⁵ According to the Premiers, an extreme vertical imbalance was promoting duplication and overlap in government services, a lack of accountability because of the break between revenue-raising and -spending, and inefficient state taxes.⁵⁶ It was also forcing the states "to pursue their self-interest above all, in order to meet the

⁵⁴ John Bannon collection, Flinders University Library, Category 044 (herein JBC), Folder: Premiers Conference 28/6/1990 (2), "News Release: State Premiers agree to Package for Premiers' Conference," 26 June 1990.

⁵⁵ JBC, Folder: [no name], "A proposal for reducing vertical fiscal imbalance," 8 November 1990.

⁵⁶ Ibid.

fiscal demands of uneven economic development”.⁵⁷ This is contrary to the notion that a high VFI would encourage cooperation as states are forced to rely on the federal government.

The problem, as noted by the Victorian government, was that

the reality of political and constitutional development in Australia is that each sphere of government has developed the attributes and responsibilities of ‘general’ government. Each government is required to take a general interest in the circumstances of its territory...The actions of each sphere of government have significant effects on other spheres...To some extent, responsibility will continue to be shared among sphere of governments.⁵⁸

Hawke concurred, noting that duplication and division of policy coordination can “distort the very design of programs...instead of serving the interests of [citizens].” He was ready to examine the untying of grants and he even announced a minor reform: the Commonwealth was going to “relinquish the bank accounts debits tax to the States”.⁵⁹ Mills (1993, p. 28) contends that Hawke was “an unfailingly creative generator of compromise proposals”. By offering to examine the VFI with the states, Hawke was demonstrating the utmost seriousness of his proposal whilst simultaneously reaching out to the states in an attempt to find compromise, which for Hawke “was never a dirty word”. In this Hawke was supported by the Business Council of Australia (1991), which advocated at the very least for a review of Australia’s governing structures, the roles of government, and their financial relationship.

It is evident from Hawke’s speech that one factor that led to COAG’s institutionalization was a change in attitude on the part of the Commonwealth. Why did it suddenly see the need to

⁵⁷ JBC, Folder: [no name], “Draft Proposals, Premiers and Chief Ministers of States and Territories in the Australian Federation,” November 1991.

⁵⁸ Public Records Office Victoria, Victorian Archives (herein PROV), Box 12549/P0003-000288, Folder: Special Premiers Conference Working Group on Tied Grants, “Strategic Overview of the Special Premiers’ Conference Agenda,” 8 July 1991, p.11.

⁵⁹ NLA, Hawke at NPC, 19 July 1990.

work with the states rather than dictate to them, as had so often occurred in the past? Why did Hawke choose this moment to move on policy duplication and on cooperative and fiscal federalism? It is also necessary to understand why the states' attitudes also changed, not only towards the Commonwealth but also towards each other. What factors contributed to their transition from competitive to cooperation federalism? Answering these questions uncovers the forces at work on Australian political actors and institutions, revealing an under-studied reason for COAG's institutionalization.

Hawke himself reveals the motivation for proposing a series of SPCs. Certain impediments and anomalies stood in the way of achieving the goals of improving national efficiency, international competitiveness, and the delivery and quality of government services. These anomalies were specified in the speech: different state schooling systems, different state licensing rules for professionals preventing ease of labour movement, different packaging rules, inconsistent transportation regulations; the examples continued to flow throughout his speech. "How sensible," Hawke asked his audience at the NPC, "is it to shrink what is already a relatively small Australian market into separate State markets?" Hawke placed these microeconomic reform issues first because they are essential "if we are to have a more competitive economy".⁶⁰ In fact, Hawke had just campaigned on this very issue. In a speech at the NPC just prior to the March 1990 election, Hawke outlined his government's vision for Australia: "an Australia with a modern, diversified, competitive and export-oriented economy; an Australia vigorously engaged with the world economy, and enmeshed in particular with the dynamism of Asia and the

⁶⁰ Ibid.

Pacific;...a self-reliant Australia, not merely fitting in with the world as we find it but helping shape it”.⁶¹ Where did this vision come from and what does it have to do with Australian IGR?

Hawke understood clearly the connection between the economy’s competitiveness and the new process of cooperation he was asking the states to undertake: “My government has acted to reform the financial system, tariffs, aviation, telecoms, taxation... - areas of virtually exclusive Commonwealth control. We still have unfinished business on our agenda. In advancing to the next stage, the co-operation of the States is essential”.⁶²

Here is revealed another key factor of the institutionalization of COAG: the Commonwealth needed the states to finish its slate of ambitious structural reforms to the Australian economy. This comes as no surprise since Australia has sovereign sub-units with powers over economic policy. Yet Australia too is one of the most centralized federations in the world (Watts, 2008). That, coupled with concurrency in the Australian constitution, should spell the end of this research: cooperative federalism is a product of constitutional design. But in fact, Australian IGR is marked by decades of competitiveness that rivalled at times the bitterness of Canadian IGR and resulted in weakly institutionalized HoG summits that were minimally routinized and not infused with much value. In theory, Australia’s institutional design and VFI should combine to encourage or even force cooperation. The reality is that genuine cooperative federalism in the form of an institutionalized HoG meeting – which is fully routinized and infused with considerable value – emerged despite these factors. What drove Australian governments to change the overriding characteristic of their HoG summits from competitive to cooperative?

⁶¹ NLA, Speech by Bob Hawke at the National Press Club, 21 March 1990 (see also <http://pmtranscripts.dpmc.gov.au/release/transcript-7984>).

⁶² NLA, Hawke at NPC, 19 July 1990.

The Lucky Country's Economy

Upon his election in 1983, Hawke's Labor government began a series of reforms that, when completed, would radically transform the Australian economy:

For 30 of the 33 years before we came to Government – [with] conservatives in government [there was] no micro-economic reform at all. The easy assumptions of the lucky country, that it was all going to fall into Australia's lap from a grateful world that loved us for some peculiar reasons, that we didn't have to do anything.⁶³

Hawke may have been in campaigning mode during this speech in 1990 but the implication of using the 'lucky country' phrase was clear: a Hawke government was all about change.

What does 'lucky country' mean and why is it significant in the context of microeconomic reform? We must turn back to a time before Hawke and the Liberal government that preceded him, all the way back to 1964. Coined by public intellectual Donald Horne (1998 (1964), p. xi), *The Lucky Country* "was written at a time...when Australia seemed to be rusting up". On the surface, the phrase denotes an attractive, pleasant, and charming country experiencing the full impact of the post-war boom. Underneath the surface, however, lies the irony behind the phrase. For Australia is not 'lucky' to have its natural environment, climate, or resources. Rather it is the opposite since these attributes contribute to apathy, particularly in a political sense, and to a lack of imagination: "Australia is a lucky country run mainly by second-rate people who share its luck" (ibid., p. xi). Horne used the phrase ironically to denote caution rather than praise.

⁶³ NLA, Hawke at NPC, 21 March 1990, Question and Answer session (see also <http://pmtranscripts.dpmc.gov.au/release/transcript-7985>). See also Conley (2009, p. 105), who discusses that both the Whitlam and Fraser governments "continued to believe that the rural and resources industries would provide for Australia's future," although Fraser did "equivocate" over tariff reductions.

There are other elements to the phrase, including racism, intolerance and illiberalism, all of which combined to create the idea of the 'Australian settlement'.⁶⁴ Of interest here is its economic warning. Horne described a suburban nation during a "self-assured period of the white picket fence [that is reliant on] jobs that would last a lifetime" (ibid.). The warning is that the Australian economy was headed in the wrong direction. Horne understood at some point that the 'turn to Asia' had to occur if Australia was to prosper economically and find some self-confidence. Future PM Paul Keating understood this too (particularly his views about ANZAC, discussed in the next chapter), which is why both he and Horne wanted the turn away from Europe to occur via the most symbolic of moments: the declaration of a republic.

Horne also understood that relying on resource extraction and tariffs to protect domestic industry was a recipe for economic disaster. He championed diversification, specifically in the tertiary economy, and noted in a revised edition that Hawke tried to balance his 'competitive Australia' reforms with 'clever Australia' programs, though the latter seemed to Horne to have fallen by the wayside. Horne noted that "our tradition is of a colonial-minded and derivative business culture, especially in manufacturing and banking" (ibid., p. xx). Relying on resources rather than creativity or imagination is why 'lucky country' is a warning, to be said with irony rather than triumph. Australia is successful because of its attributes yet it risks becoming "a rundown, old-fashioned, puzzled, and resentful [nation]" (ibid.). Its leaders are second-rate because "their imagination seems exhausted by the country's achievements" (ibid., p. 13), which is not helped by the fact that Australia "is an extraordinarily stable society" (ibid., p. 17). The

⁶⁴ The phrase refers to protectionism along with a 'white' immigration policy, wage arbitration, state paternalism and Imperial benevolence, hence why 'lucky country' encompasses more than just economics; see Kelly (1994).

stability stemmed from post-war full employment, low inflation, and sustained economic growth. Stability makes Australians skeptical of change hence the seeming lack of substantial change under Liberal governments; when change does occur, it is organic and pragmatic (ibid., p. 34). The implication is that changing Australia requires instability; it requires a crisis.

The warning in Horne's 1964 classic was thrashed in policy circles before eventually directly confronting Australia's governments. Industry associations and the Trade Ministry were positioned against the Tariff Board, economists, journalists, and some politicians, notably Burt Kelly. He was a Liberal Party backbencher and short-lived Cabinet Minister who became an early advocate for free trade, which he outlined in his 'Modest Member' and then 'Modest Farmer' columns in the *Australian Financial Review*.⁶⁵ The Trade Ministry and its supporters defended the ability of tariffs to promote economic growth whilst their opponents espoused the benefits of free trade and demanded transparency in setting tariff rates (Snape et al., 1998, p. 20). Little changed until the economic crisis of the 1980s was fully evident.

At the centre of the debate was the 'Fortress Australia' mentality. Into the 1960s, the Vernon Report viewed tariffs as necessary for both economic and income growth. The justification used by politicians was that Australia was in a midway position vis-a-vis world trade (Snape et al., 1998). Midway refers to its status as a developing economy, because it did not have a fully industrialized economy, and to elements of its economy that are characteristic of developed economies, such as its cost disability, i.e., its wages and standard of living were so high as to render its industry uncompetitive. Only protectionism could address the midway issue.

⁶⁵ See Colebatch (2012).

The policy debate culminated in the first round of tariff reductions in 1973, a one quarter cut across-the-board, by Gough Whitlam's short-lived but active Labor government. However, issues other than economic reform demanded the government's attention:

In his first ten days alone...[Whitlam] crossed off well over half of his to-do list: got Australia's last troops out of Vietnam, ended conscription, and set up commissions to look into school funding, equal pay and aboriginal land rights....[By the end of his prime ministership] he had brought in a state-funded health system [known as Medibank]...; no-fault divorce laws; electoral reform, tariff reform, votes at 18 and free university education. He had also given Papua New Guinea independence and opened up relations with China. No wonder the general view, in his opinion, was that he was the best prime minister Australia had ever had" (The Economist, 2014).⁶⁶

Whitlam's reform era was short-lived due to the Dismissal in 1975, when the Governor-General asked then Opposition leader Malcolm Fraser to form the government when Whitlam could not pass a budget through the Senate. It was not until the Hawke Labor government in 1983 that the challenge to act on the economy that Horne had issued was taken up. But the Whitlam era did give credence to a slowly developing realization across Australian society that change was needed. Whitlam's dismantling of certain parts of the 'Australian settlement' meant that it was only a matter of time before protectionism too was discredited (Snape et al., 1998, p. 9).

The task was not the politician's alone. The Australian people, labour unions, and employers needed to change too. According to Horne, whilst the elites may have been second rate, the Australian people are adaptable; "the potential for change within the ordinary people of Australia is great" (Horne, 1998 (1964), p. 41). As Hawke stated in 1990, "we've got now a receptive, cooperative trade union movement. We've got a much more enlightened band of

⁶⁶ See also McDougall (2015).

employers, collectively and individually and government, State governments also. [The] hard battle of changing attitudes has been won”.⁶⁷ How was this accomplished? Hawke’s personality was key. He was a consensus-builder: “his ability to overcome the divisiveness of the previous years [is] a key element in achieving change” (Bloustein, Mackinnon, & Comber, 2009, p. xii). Mills (1993) also describes Hawke’s love affair with the Australian people; former NSW Premier Neville Wran described Hawke’s entry into politics as “manna from heaven, the elixir of life” (Chubb, 1993, p. Ep.1 4:09). Horne’s belief that Australian leaders are second rate may have been overturned by Hawke and his unprecedented four back-to-back election wins. With first rate leadership, the Australian people for a time lived up to Horne’s assessment of their adaptability.

Horne’s diagnosis of the Australian economy in 1964 was no less relevant in the 1980s. Australia has been a small open economy since its colonization.⁶⁸ It has always been a price-taker, i.e., it has relatively little impact on world markets even though it relies so heavily on them (Kriesler, 1995). When taken to the extreme, Australia’s position in the world market has devastating effects on its ability to stay competitive and prosper when debts and imbalances are not properly managed.

Indeed, by the 1980s, current account deficits and the resulting increase in foreign debt were hamstringing economic growth. Traditionally, Australia has had a current account deficit owing to the fact that it imports more than it exports (Kriesler, 1995). When prices for its commodity exports were high, the deficit was manageable. But by the 1980s, relying on resources was no longer a solution, rather it was the source of Australia’s problems. The 1980s

⁶⁷ NLA, Hawke at NPC, March 1990 Q&A, p.3.

⁶⁸ See McLean (2012).

were characterized by low commodity prices and sluggish growth worldwide and also high inflation and the accompanying high interest rates that were meant to contain it. Meanwhile, Australians were paying higher prices because of their heavy reliance on imports, which was due to a lack of domestic competitiveness and investment coupled with high domestic demand and a high Aussie dollar. Add in increasing government deficits and the result was foreign debt approaching 30% of GDP in 1986 (EPAC, 1986a, p. 1) and 42.9% by 1993 (Kriesler, 1995, p. 8).⁶⁹ Treasurer Keating became convinced that the level of debt was a serious problem in May 1986, when the Reserve Bank advised the government to focus on the current account imbalance, which reached A\$1.35 billion by May 1986. This was “a pivotal point...where the Hawke government was forced to change course, abandon the high growth targets and knuckle down to solving the country’s deep-seated economic problems” (Carew, 1992, p. 170).

Australia’s export/import imbalance and sluggish domestic competitiveness were growing increasingly evident. For one, Australian productivity growth was below the OECD average between 1970 and 1987 (Dao, Ross, & Campbell, 1993). Investment in the Australian economy was not creating an internationally competitive export base; Australia was not taking part in the worldwide expansion of trade: “In contrast to the outward-looking policies of East Asia, Australia has a legacy of inward-looking industrial policies”. In fact, exports as a share of GNP stagnated for over twenty years: 14% in 1962 compared to 13% in 1981. Stagnant trade was tied to lackluster growth: “Australia has slipped from third highest in the 1950s to below tenth in terms of per capita incomes” (EPAC, 1986b, p. 5). Its growing foreign debt was directly related

⁶⁹ Cost of servicing the debt went from 5.4% of GDP in 1981 to 26.3% in 1991. By comparison, Canada’s debt-to-GDP ratio in 1993 was 68.4% (see Veldhuis, Clemens, & Palacios, 2012).

to its poor trade performance (Kearney, 1993). The reason for its poor showing was, once again, its overreliance on resources. Growth in world trade was taking place in the manufacturing sector (machinery and transport equipment were the fastest growing at the time) yet Australia relied on primary goods in agriculture, energy, and minerals whose markets were increasingly competitive, causing prices to fall: “60% of the shortfall between the rates of growth of Australia’s exports compared to the whole world is accounted for by the difference in the composition of our trade” (EPAC, 1986b, p. 12). The situation was so untenable that Keating referred to Australia as a potential ‘banana republic’.

How could Australia rely so heavily on international markets yet take no part in an expansion of global trade? It was due to the ‘Fortress Australia’ mentality. The windfall from commodity goods after WWII allowed Canberra to raise tariffs on just about everything else in an attempt to stimulate domestic production. The result was an uncompetitive and backward industrial base.⁷⁰ “We failed to develop a capital goods sector and the complex input-output relationships between the major sectors of our economy which are the key hallmarks of a truly industrialised economy” (Kriesler, 1995, p. 146). Rather than help Australia emerge from its midway status, ‘Fortress Australia’ achieved the opposite: Australia was unable to respond quickly to changing international economic conditions (Dao et al., 1993). Domestic industrial efficiency and competitiveness, i.e., a truly developed and industrialized economy, were sacrificed in order to maximize commodity production and achieve full employment. Australia was the ‘lucky country’ indeed.

⁷⁰ Import substitution is generally only good in the short term before industries begin to stagnate (see Marks, Hettihewa, & Sadeghi, 1998).

The First Three Hawke Labor Governments

Addressing the lucky country's challenges required nothing less than a complete reorientation of the Australian economy: more domestic production, investment, and saving coupled with more and diversified exports (EPAC, 1986a). Improving domestic competitiveness was also required (EPAC, 1986b). All of these amounted to internationalizing the Australian economy.⁷¹ Relying on worldwide shifts to force change could help – as it did in the past – but it would not solve the underlying competitiveness and productivity issues facing the economy. This time around, waiting for higher prices and more demand for commodities was not going to work. Sir John Crawford's report in 1979 stated that if Australia was to prosper, it had to cut tariffs and build an export-competitive manufacturing sector that could take advantage of Asian markets. One of the authors of that report was union leader and future PM Bob Hawke (Mills, 1993).⁷² As shadow minister for minerals and energy, Keating stated his purpose after the election was to understand "why was [the Australian economy] performing so badly; why were we condemned to such low growth? So I was trying to find the codes and what a Labor policy would be...to make the link between labour and capital...to [have capital] pull labour in its stead" (P. Keating, 2013, p. Ep.2 6:21) .

When both men were in government after the March 1983 election, they enacted several reforms to address Australia's imbalances. The first significant reform was wage restraint: "Real wage restraint, accompanied by such massive improvement in the social wage – the restraint

⁷¹ See Athukorala (1998).

⁷² The Reserve Bank of Australia commissioned a conference on the sources of reform (see Gruen & Shrestha, 2000).

with equity...that has been so magnificently provided by the Australian community – has set the course for growth”.⁷³ Curbing wages helped to reduce inflation and increase Australia’s competitiveness. The policy would then be accompanied by debt reduction (J. Edwards, 1996).

As a former union leader, achieving labour peace and reconciliation was an important personal goal for Hawke (Bloustein et al., 2009). Hawke stated,

the basic problem confronting Australia when we went up to the 1983 election was that we had an Australia that was bitterly divided. So reconciliation was the basis of everything...We had to have recovery...because we were in a serious recession...and out of that we had to have a reconstruction of the Australian economy...[the] three Rs.” (Chubb, 1993, p. Ep.1 16:30).⁷⁴

Hawke brought together Australian governments and the representatives of both labour and employers at the National Economic Summit on 11 April 1983. Back in January, Hawke had proposed the summit as a “process of knowledge acquisition and sharing” between stakeholders to analyze the economy, specifically wage and price movements.⁷⁵ Hawke acknowledged that combatting Australia’s economic crisis, particularly unemployment levels not seen since the Great Depression, required avoiding going “down the path of confrontation and fragmentation which has embittered and disfigured so many aspects of national life”.⁷⁶ Keating and others in the Labor Party⁷⁷ were at first skeptical of the Summit’s ability to contain wage growth (J. Edwards, 1996). But the Summit was only the beginning of the process: “Beneath the shiny

⁷³ NLA, Speech by Bob Hawke at the National Press Club, 7 December 1989 (see also <http://pmtranscripts.dpmc.gov.au/release/transcript-7849>).

⁷⁴ P. Keating (2011) described it as needing growth and productivity to shift national income to Labor’s constituency.

⁷⁵ Bob Hawke Prime Ministerial Library, University of South Australia (herein BHPML), Address by Bob Hawke to the National Economic Summit Conference, House of Representatives, 11 April 1983, p.2.

⁷⁶ Ibid., p.3.

⁷⁷ The Premier of NSW at the time, Neville Wran, thought that “consensus was fanciful” but in retrospect he believed the attendees embraced it because of “Hawke’s special magic” (Chubb, 1993, p. Ep.1 27:25).

chrome plate of national consensus lay the steel of Labor's tough new economic strategy" (Mills, 1993, p. 37). Hawke was so convinced of this that he quoted wartime PM John Curtin's praise of the quality of Australians in meeting the challenge of war. For Hawke, the economic crisis was a grave modern challenge: "If we at this conference dedicate ourselves to provide leadership to this great people...they will respond with a united effort and renewed determination to beat this crisis".⁷⁸

The Summit succeeded in drawing up the Prices and Incomes Accord, which the summit process legitimized.⁷⁹ Rather than sector-negotiated wages, a national Industrial Relations Commission would oversee negotiations for the bulk of the workforce. Along with labour peace, it was an anti-inflationary measure that, along with tax reform, sought to keep after-tax wages stable. It also set a deficit target, eliciting support for longer term deficit reduction since the Accord and tax reform would prevent cuts to take-home pay (J. Edwards, 1996). It failed however to stimulate productivity growth even as Australia saw "faster job growth...than in most other wealth industrial economies" (J. Edwards, 2000, p. 29). Thus, the Accord eventually outlived its usefulness but for 10 years it was the cornerstone of Labor's economic policies.

For the moment, labour peace was needed for what was to occur next: cutting tariffs on imports. The existence of tariffs was increasingly difficult to justify because significant tariffs covered only approximately 20% of manufacturing employees. They were also ineffective at protecting workers from job losses during recessions (Conlon, 1998). Victoria, the most protected state, remained in the economic doldrums well into the 1990s. Cutting tariffs would

⁷⁸ BHPML, Hawke to National Economic Summit, p.10. See Anson (1991) for a Hawke-Curtin comparison.

⁷⁹ According to Bill Kelty, then Secretary of the Australian Council of Trade Unions (Chubb, 1993, p. Ep.1 29:45).

open up Australia's sheltered industrial base and force it to restructure along more efficient and productive lines. Whilst good for the overall economy – owing to a decrease in the prices of inputs and consumer goods – it was potentially very bad for workers in uncompetitive industries. In fact, some of the most protected and labour intensive industries – cars and textiles – were spared from the first round of cuts.

By the mid-1980s, the effective rate of assistance to industry was less than half that of the early 1970s (Athukorala, 1998). Keating's May 1988 economic statement continued to reform a tariff system he believed left untouched would eventually turn Australia into a 'banana republic'. Tariffs, he said, led to "a less flexible economy, too reliant on protection and regulation". Changes over the next four years saw tariffs fall to a maximum of 15%, amounting to a cut of 20% in average protection levels. Once again textiles and cars were exempted. These cuts would improve efficiency in industry and promote structural changes and investment in internationally competitive sectors (Snape et al., 1998, p. 85). Up to this point, the Commonwealth was undertaking microeconomic reforms that were completely within its constitutional remit.

After wages and tariffs, the third set of reforms was to the financial sector. Opening the banking sector to competition was critical to improving investment. The groundwork had been laid by the outgoing Fraser government and so the Liberals provided political cover for these changes (J. Edwards, 1996). After considering 42 applications, 16 foreign banks were invited into the Australian market (Carew, 1992). Restrictions on foreign investment were also lifted.⁸⁰ It was a massive shock and a complete reversal of Labor Party orthodoxy. Keating confronted his

⁸⁰ BHPML, Speech by Bob Hawke, "Micro-Economic Reform: the Fourth Term Agenda," 22 February 1990, p.11.

opponents at the July 1984 Labor Party conference: “If you want to start talk about equity and fairness, you better start with unemployment. But you can’t do it with a sick economy. Banking is the artery of the economy and we’ve had hardening of the arteries for too long in this country” (Chubb, 1993, p. Ep.1 43:08).

Floating the dollar and lifting exchange controls were major reforms, undertaken despite having the effect of exposing the Australian economy to further commodity price fluctuations and currency swings, both of which contributed to the jump in Australia’s foreign debt during the 1990-91 recession. However, the exposure to price swings was actually exposure to the discipline of international finance; floating the currency was a necessary step in righting the economy’s overall imbalances: “the net result is to encourage a more diversified economy” (Bloustein et al., 2009, p. 168). Most especially, a lower dollar coupled with wage restraint helped to boost Australia’s competitiveness and initiate further reforms to tariffs and the banking industry.⁸¹

As well, the Reserve Bank was simply too small in relation to foreign currency markets to sustain a fixed level for the Australian dollar for any significant period of time. The problem was that the Reserve Bank “opens its shop every Monday morning at 9 o’clock and buys all the foreign exchange and then issues Australian dollars. Those dollars just pumped up the money supply and added kerosene to inflation. It was all wrong” (P. Keating, 2013, p. Ep.2 23:05). Allowing the currency to float transformed the mission of the Reserve Bank from controlling the exchange rate to stabilizing interest rates, which would assist with controlling inflation and lead to higher

⁸¹ See J. Edwards (1996) for a full account of these reforms. To this day, Hawke and Keating disagree on exactly how the decision to float came about. Truth be told, such a major reform required them both.

investment in industry (Athukorala, 1998). The reforms also provided a “useful rhetorical device to persuade Australians about the urgency of change” (Conley, 2009, p. 133). These reforms were executed with some trepidation. Barbara Ward, former adviser to Keating, recalled that “after it became clear that the currency was going to be floated irrespective of [the views of The Reserve Bank and Treasury]...[they] stood up and left the meeting, basically taking the attitude ‘on your head be it’” (Chubb, 1993, p. Ep. 1 37:18). The short-term results would confirm the trepidation, forcing the government to undertake microeconomic reform.

Microeconomic Reform

The reforms discussed above were designed to foster radical economic change. The reforms and the rhetoric behind them were needed to affect “a re-orientation of Australian management and for improvements in the skill base” (EPAC, 1986a, p. 2). Business had to change but they needed government assistance to improve productivity and restrain wages. Hawke declared that businesses “are the front line troops” in replacing imports with exports.⁸² Government needed to provide the right policy environment for change, to restrain deficits, and support an industrial policy that assisted export diversification – what Li (2015) refers to as state-society synergy. Short term fiscal restraint was helping to cool domestic demand but it would be long-term reform that really mattered: “The solution lies in a re-structuring of the supply side of the economy and lifting of Australia’s underlying productive capacity, particularly in the export sector” (EPAC, 1986a, p. 47). Microeconomic reform was needed to alleviate constraints on domestic activity and redirect investment flows to an internationally competitive industrial base:

⁸² BHPML, Speech by Bob Hawke at the Annual General Meeting of the Business Council of Australia, 18 October 1990, p.14.

“From 1987 Keating spoke out strongly for faster micro-reform, including tariff cuts” (J. Edwards, 1996, p. 333).

Microeconomic policies primarily manage the efficiency of the economy in several areas, including firm resource utilization, industry-level resource allocation, technology and skills investment, and the speed of adaptation to changing competitive environments. Many government policies are involved, including education, business and licensing regulations, industrial policy, tariff schedules, transportation and communication infrastructure, and the labour market (Kriesler, 1995). With higher efficiency comes higher productivity and increasing returns of scale, all of which increase overall competitiveness (Athukorala, 1998). Further benefits included lower prices, improved reliability, better quality and more choice in goods and services, more competition, higher government income, higher employment, and improved working conditions (Filmer & Dao, 1994).

Microeconomic reform took centre stage on the Commonwealth’s policy agenda after its macro-economic management of the economy partially failed to achieve domestic competitiveness: “Having removed one layer of protection, the government aimed to reduce the overall cost of production by lowering domestic barriers” (Bloustein et al., 2009, p. 170). Into Hawke’s third government, inflation and unemployment remained stubbornly high and the current account was still in deficit. Reforms to the macro-economy had seemed to only make things worse nor was the situation helped by the 1987 stock market crash. It was a “terrible” time for Keating considering that he was so close to “declaring a victory over the almost maliciously perverse Australian economy” (J. Edwards, 1996, p. 362). In the end, exposing the

Australian economy to more competition was not enough to force change.⁸³ Concerns were now turning to “the cost to business and the economy...of unnecessary or/and poor quality regulation at both state and federal levels” (Carroll & Head, 2009, p. 3).

Conley (2009, p. 107) writes that by 1986

Australia was in almost terminal decline...The sense of crisis framed economic policy for the rest of the 1980s, reinforcing the government’s belief that fundamental economic restructuring was unavoidable and that widespread liberalisation – beyond the financial sector – was the only realist policy response.

The situation stemmed from the terms of trade crisis. On 13 May 1986, current account figures for the previous month showed a massive deficit, \$A1.4 billion, a swing of almost A\$450 million in just one month (Chubb, 1993, p. Ep.2 37:20). The next day, in a radio interview, Keating compared Australia to a ‘banana republic’.⁸⁴ The statement sent shock waves through the country but it also “foster[ed] an acceptance in the broad community that the country was in difficulties” (Carew, 1992, p. 172).

The release of the figures and Keating’s comment is a critical juncture both for its economic and political implications. Keating’s ‘slip of the tongue’⁸⁵ over the phone in a restaurant kitchen caused a rift between himself and Hawke. It was a significant moment in their relationship, when Keating realized that he was the driver of reforms and had to take Hawke with him (Chubb, 1993, p. Ep.2 46:00). The surprise figure forced a rewrite of the 1986 budget. The

⁸³ EPAC concurred when it reported that both the trade-exposed sectors and non-trade exposed sectors required reform (see EPAC, 1991a).

⁸⁴ See Snape et al. (1998). A banana republic is a politically unstable country that relies on exporting a limited number of resources (such as bananas). Keating said to the radio presenter, “If this government cannot get the adjustment, get manufacturing going again and keep moderate wage outcomes...then Australia is basically done for. We will just end up being a third-rate economy”. When quizzed whether a lack of reform meant a depression, Keating responded: “Then, you have gone. You are a banana republic” (quoted in Carew, 1992, p. 172).

⁸⁵ See J. Edwards (1996).

printing presses were stopped and, within two weeks, A\$1.5 billion of cuts were announced. Former Minister of Education Susan Ryan described the Cabinet committee during that time as an “aggressive environment” (ibid., Ep.2 49:45). Keating’s attempt to declare victory over the Australian economy would have to wait a while. Further surprises were still in store: their efforts in reduce the deficit in 1986 led to the 1988 budget, which recorded the largest surplus in Australian history and was supposed “to bring home the bacon” only for the Australian economy to begin a deep recession in 1990 (ibid., Ep.3 34:50).

The perception of economic crisis from Keating was an important reason why microeconomic reform found expression shortly thereafter. The other causes, according to Gerritsen (1992), were the tariff cuts and support from the policy community. In 1987, Hawke announced microeconomic reforms to transportation, communications, and the unions. These were part of the mission of reconstruction: “transforming the nation from the complacent Lucky Country to the productive country, the innovative and hard-working country” (Hawke, 1994, p. 411). In August 1989, Keating announced changes to the Industries Assistance Commission (formerly the Tariff Board), now to be called the Industry Commission, which was “to function as a broader-based micro-economic reform review agency [which would serve as] ‘a catalyst for dynamic change in industry’” (Carew, 1992, p. 261). According to Keating, microeconomic reform was designed to open up the product markets, which followed from the policies that liberalized the labour and financial markets: “the whole internationalization of Australia would have stopped stone dead if we’d have had flexible financial markets but rigid product markets” (P. Keating, 2013, p. Ep.3 17:45).

'Turn to Asia'

The crisis in the current account was due in part to fundamental shifts in the Australian economy, what is today referred to as the 'turn to Asia'. The Garnaut (1989) Report took up the cause of diversifying Australia's exports and developing a sophisticated industrial base in order to counter the deficit crisis.

The growth being experienced in North East Asia was a tremendous opportunity for Australia. Its location moderated Australia's relative isolation and its countries were economically complementary given that Australia's resources are important inputs into Asian manufacturing and that Asian savings were a significant new source of foreign investment. As well, Australia's technical skills, R&D system, educational capabilities, and its tourism potential were necessary or desired by Asian businesses and Asia's rising middle class (Garnaut, 1989, p. 2). By taking advantage of all these opportunities, Australia could succeed in diversifying and increasing its exports.

The task was monumental since protectionist policies had robbed the economy of approximately \$A20 billion a year worth of exports (ibid., p. 206). Reversing this trend required speeding up the reduction of tariffs, a major recommendation of the Garnaut Report. Domestic reforms that lowered the costs of trade and increased competitiveness were also necessary to further internationalize the Australian economy. Garnaut's specific analysis of the processed raw materials industry noted that it had lost competitiveness but that microeconomic reform to electrical grids, environmental regulations, and the waterfront could restore the industry and propel growth given the projected growth of the Asian economies (ibid., p. 229). As well, government deficits needed to be lowered and foreign investment rules relaxed in order to reverse the current account deficit. More broadly, Australian governments needed to reform

education so that business managers and the public in general were more familiar with their Asian neighbours (see *ibid.*, Chapter 15).

Garnaut wrote that reforms to the macro-economy, such as floating the dollar and removing most banking restrictions, had helped but that the benefits had come slowly: “The danger is that slow change may bring gains too slowly to consolidate community support for them...This danger would be less the clearer and wider community understanding of the long-term end points of change” (*ibid.*, p. 210). Hawke received the message and made the Report’s recommendations, along with its advice about community support, a significant aspect of his 1990 re-election campaign. Garnaut also succeeded in garnering the approval of his academic colleagues. Whilst they took issue with some of his assumptions, most if not all broadly agreed with his proactive conclusion that Australia needed to fundamentally reorient not only its economy but its society, politics, and foreign policy as well.⁸⁶

Senior bureaucrats familiar with COAG stated clearly that the “Asian century requires federal-state coordination”.⁸⁷ The problem with managing the ‘turn to Asia’ was not necessarily the existence of overlap and duplication between governments but whether sufficient governance structures were in place to manage the issue and its inherent inefficiencies. Was the Australian IGR system up to this task in a new economic environment? Prior to the establishment of COAG, the answer was no. The ‘turn to Asia’ represented the solution to Australia’s economic woes, which had forced the competitiveness and economic governance issues onto HoG’s policy

⁸⁶ See Richardson (1991). Most interesting is the criticism that Garnaut viewed the state as neutral with regard to the composition of growth. Furthermore, Garnaut is criticized for relying too heavily on NE Asia and for glossing over their non-tariff barriers to trade, hence the growing importance of SE Asia.

⁸⁷ Interview with former government official, 18 July 2014.

agenda. Whereas the Premiers' Conferences only considered financial issues, the present economic problems and their solution required addressing a broader set of issues, hence the formation of the SPCs. Here then is a significant reason for the institutionalized of COAG: competitiveness and internationalization were the policy goals of every Australian government. Achieving these goals meant building stronger IGR institutions.

There was also an external relations element to the 'turn to Asia'. With the EU continuing to evolve and the North American Free Trade Agreement (NAFTA) taking shape, Australia was concerned that it would find itself alone and isolated in a world of trading blocs. It was already being squeezed by the US-Europe trade war. In light of the situation, the Hawke government sought to strengthen its hand in the Uruguay round of trade negotiations by establishing and chairing the Cairns Group in 1986. Made up of agricultural fair traders seeking free(er) trade, this group of countries represented an overwhelming bulk of the world's agricultural exports outside the EU and USA (Hawke, 1994). The group failed to immediately resolve the agricultural trade issue⁸⁸ and so Hawke sought to further strengthen other multilateral processes: "I wanted now to bring together my two fundamental and interrelated themes of a freer international trading environment and Australia's greater enmeshment with the region" (ibid., p. 429). In a speech in Seoul, South Korea on 31 January 1989, Hawke proffered the idea of what would become the Asia Pacific Economic Co-operation (APEC) forum. At its first meeting in Canberra in November 1989, Hawke conceded that Australia had been economically and politically insular towards its Asian neighbours, "but those days are gone – gone forever...[O]ur future is thoroughly interwoven with that of the Asia Pacific region" (Conley, 2009, p. 146). Debate continued for over

⁸⁸ The Uruguay Round did not wrap up until 1993.

a decade on whether APEC was merely a talking shop or was actually liberalizing multilateral trade. Pomfret (1996) argues that notwithstanding the debate, Australia became actively involved in Asian diplomacy whilst Sheehan (1996) sees Australia as a vital link between east and west.⁸⁹

Conjointly with the government's tariff reductions was its promotion of exports. The complementarity of tariff reductions and export promotion was included in the 1977 White Paper on Manufacturing (Snape et al., 1998, p. 261). Meagre sums and the deterioration of the current account led the Hawke government to review its export promotion schemes. Rather than simply assisting tariff reductions, the Ferris Report expanded the purpose of export promotion to include internationalizing the whole economy. The highlight of reforms was the creation of the Australian Trade Commission (Austrade). Its aim was to implement industry-specific export promotion schemes, otherwise known as microeconomic reform: "Such aggressive export promotion was consistent with the Hawke government's emphasis on the need for radical change in outlook epitomised by the Treasurer's 'Banana Republic' comments" (Snape et al., 1998, p. 264). The 1989 Hughes Report argued that a microeconomic reforms and an export-conducive macro-economic environment were better at promoting exports than direct assistance but that ending export promotion schemes at such an early stage of the overall reform process would send the wrong signal. "If the pace of microeconomic reform...is maintained, in five years' time Australian exporters will be working in a much more productive and cost effective environment" (ibid., p. 284).

⁸⁹ See also P. Keating (2000) in which he argues that Australia is neither Asian nor European.

Diversifying exports away from resources meant, among other things, a corresponding increase in services industry exports, which also required microeconomic reform. This was underway by the mid-1980s but not nearly to the extent required to solve Australia's economic woes. Between 1970 and 1985, services as a percentage of GDP increased from 49% to 53% whilst its share of total employment rose from 56% to 67%. Services were 15.5% of total exports in 1986 (EPAC, 1987).⁹⁰ Diversifying the economy and exports sufficiently enough to solve the balance of payments problems required industries and governments to focus on "quality of service, reliability of service delivery, tailoring the service to the customer and provision of the service at a time and location convenient to the customer" (EPAC, 1987, p. 7). Hawke's consensus based policy-making body (Bramston, 2003), the Economic Planning Advisory Council (EPAC), was recommending supply side changes to the economy.⁹¹ Barriers to services trade included policies within the jurisdiction of both the Commonwealth and states, including immigration and health requirements, professional standards recognition, and security regulations. Increasing exports of services required coordination between the orders of government in all of these areas (EPAC, 1987). Privatizing sections of the services industry, including Qantas airlines and telecommunications, was also a significant reform.⁹²

Prior to the 1990 election, Hawke, on his 60th birthday, was trumpeting the realization that "we're doomed to further and further decline" if dependence on resources continues. These issues go past the next Australian election, he told reporters at the NPC. Whether on rising

⁹⁰ Services were exported to the USA (16.8%), UK (15%), NZ (12.2%), Japan (11.6%), ASEAN (10.5%) and the non-UK EC (10%).

⁹¹ Former Chief of Staff to the Victorian and NSW Premiers, Ken Baxter, believed one lesson of the reforms of the 1980s was "that an intellectually rigorous, courageous, independent national body is essential to maintain the intellectual and administrative arguments in support of economic and social reform" (Baxter, 2012, p. 6).

⁹² See Browne (2001); Hodge (2003).

interest rates or falling wages, each one of these issues was part of the greater project of reorienting the Australian economy: “That is not a simple message. But irrespective of the electoral cycle, it’s a message which if Australians don’t understand...then Australia would be doomed”.⁹³ During the Q&A, Hawke was asked about microeconomic reform. A journalist noted that progress seemed to be lacking. Hawke’s answer discussed getting all parties involved: “We will try and get the agreement of those involved for the changes that are necessary and hopefully we’ll always be able to get it”. The states were not mentioned in this discussion, just the hope of getting an agreement; if that was not possible, then “we won’t shirk taking the decisions that may be necessary in those circumstances”.⁹⁴ Hardly conciliatory or cooperative language. Party system integration and the VFI were of no consequence here.

With the election scheduled for 24 March, the campaign was well underway when Hawke released his government’s agenda for its fourth term. Fundamental to his goal of “shak[ing] out of the old complacent dependence on commodity exports” was microeconomic reform.⁹⁵ Achievements had already been secured but there was plenty more to come in aviation, railways, road, telecoms, shipping, and industry. What was not mentioned was that the cooperation of the states was required in some of these areas. Hawke also pledged to give the Garnaut Report’s recommendation on speeding up tariff cuts a thorough review upon re-election.⁹⁶ Electricity reform was to be studied, which will provide “a powerful weapon with which to combat resistance to reform from State and other interests”.⁹⁷ Once more the states are portrayed as

⁹³ BHPML, Transcript of Question and Answer Session, National Press Club, 7 December 1989, p.3.

⁹⁴ Ibid., p.13.

⁹⁵ BHPML, Speech by Bob Hawke, “Micro-Economic Reform - the Fourth Term Agenda,” 22 February 1990, p.1. See also Carew (1992).

⁹⁶ Ibid., p.4.

⁹⁷ Ibid., p.5.

obstacles rather than as partners. Nevertheless, Hawke was re-elected to an historic fourth term in government.⁹⁸

Altogether, Hawke undertook a series of reforms that drastically altered the Australian landscape. A change in economic thinking is considered the single greatest contribution made by the Hawke government: “Australians could meet the challenge of responding to international markets” without destroying their belief in ‘fair go’ (Bloustein et al., 2009, p. 175). His objectives were the 3Rs: “national reconciliation, national recovery, national reconstruction”.⁹⁹ Into the 1990s, he would find that even though significant progress had been made, none of these three goals had been achieved. The 1990-91 recession proved to be a significant catalyst for further reform; “it was the recession we had to have”, according to Keating (Chubb, 1993, p. Ep.4 34:15; I. Macfarlane, 2006). Part of the problem with reconstruction was that it required Commonwealth-state cooperation. Yet at this time, governments were in a period of restraint and the two orders of government were locked into rather heated debates on how to disperse the available funds. At the June 1990 Premiers’ Conference, Hawke’s reform plans were in tatters.

Fiscal restraint and the 1990 Premiers’ Conference

Premier Bannon of SA and Treasurer Keating had a frank discussion prior to the June 1990 Premiers’ Conference. Even though Labor had just won re-election, Keating noted “if the Current Account can be turned around, the re-election of all Labor Governments will be assured”. With

⁹⁸ Hawke’s victory was heavily reliant on environmental groups using their preferential votes to support Labor. The 1990 election recorded the highest third-party vote ever in an Australian election (McAllister, 2002). It was described by both party leaders as the most important election for 40 years (Chubb, 1993, p. Ep.4 23:48).

⁹⁹ See Hawke (1984).

Keating next-in-line to take the Labor leadership, no doubt he was wondering about re-election. Yet the quote is also indicative of the fact that Keating was determined to see through austerity and return the current account and government balance sheet to surplus. SA officials noted that “[the current account] dominates his thinking in relation to the Premier’s Conference [and it], not [Opposition leader] John Hewson is their main enemy”. Fixing the current account required fiscal restraint and microeconomic reform. Bannon “told the Treasurer that the Commonwealth needed to talk to the States who controlled the areas in which the need for reform was the greatest...it was not possible for the Commonwealth to demand reform, without giving the States more assistance”.¹⁰⁰ Keating was more focused on restraint. In a press release the day before the Premiers’ Conference, Keating stated that “fiscal policy has been the bedrock upon which the Government’s economic policies have been founded”.¹⁰¹ To stimulate private investment, the government initiated wage restraint, tax cuts, and macro- and micro-economic reforms. With a recession underway, fiscal restraint was needed to reverse the current account deficit and tackle inflation. Under no circumstances was Australia going to become a ‘banana republic’ under his watch. Yet the intense focus on these indicators was a key cause of the 1990-91 recession, which saw the highest unemployment rate in the post-war era. The Commonwealth’s policy of raising interest rates was designed to rein in the high investment and spending rates of the late-

¹⁰⁰ JBC, Folder: Premiers Conference 28/06/1990 (1), “Notes of Meeting between the Premier and the Federal Treasurer Paul Keating,” 4 May 1990.

¹⁰¹ JBC, Folder: Premiers Conference 28/06/1990 (2), “Statement by the Treasurer, the Hon P.J. Keating MP – Economic Context of the Premiers’ Conference,” 27 June 1990.

1980s.¹⁰² Instead, the terms of trade and monetary policy lag inflicted a deep recession (EPAC, 1992).¹⁰³

Meanwhile, the states were attempting to maintain public services and deal with spending cuts. Whilst in Europe, Premier Greiner announced that NSW would in fact increase its borrowings and would not cut services or increase taxes, as was being advocated by Treasurer Keating. Part of the reason was to raise investor confidence and forestall the chance that “overseas investors would not renew their NSW Treasury bonds” (Hancock, 2013, p. 250). At the June 1990 Premiers’ Conference, Bannon’s opening remarks confirmed his government’s fiscal restraint in response to the recession. Even if the Commonwealth did not cut transfers, “SA is likely to have serious budgetary difficulties”.¹⁰⁴ In a letter to Hawke, Bannon was more direct: “we understand, and in general terms support, the Commonwealth’s expenditure restraint policy. But we need time to adjust. Our budget outlook for 1990-91 is nothing short of disastrous”.¹⁰⁵

Bannon’s effort to maintain social justice programmes without hiking state taxes occurred in tandem with efforts to reduce costs to consumers through microeconomic reform of electricity markets and through efficiency gains in the public service.¹⁰⁶ Keating’s pre-conference press release also highlighted areas that needed microeconomic reform, notably transportation, which significantly weighed on state budgets. He stated that a Commonwealth program of

¹⁰² See J. Edwards (1996) for these interest rate decisions.

¹⁰³ EPAC (1992) concluded that half of the cause of the recession was due to these factors, the other half potentially from the dollar float, financial deregulation, and the short-term costs of microeconomic reform, costs which Filmer and Dao (1994) later conclude were justified because of their long-term benefits.

¹⁰⁴ JBC, Folder: Premiers Conference 28/06/1990 (2), “Premiers’ Conference Opening Address,” 28 June 1990.

¹⁰⁵ JBC, Folder: Premiers Conference 28/06/1990 (2), “Letter from Bannon to Hawke: Financial Issues between the Commonwealth and South Australia,” 22 June 1990.

¹⁰⁶ JBC, Folder: Premiers Conference 28/06/1990 (2), “Premiers’ Conference Opening Address,” 28 June 1990, p.3.

microeconomic reform was forthcoming and that “a comprehensive and concerted effort necessarily involves the States [and] that the Commonwealth will seek to begin a process at the Premiers’ Conference to address microeconomic reform at the State level”.¹⁰⁷ In a letter to Hawke, Greiner welcomed the Conference’s agenda, which sought the states’ cooperation on microeconomic reform as well as a review of functional allocations.¹⁰⁸

Yet Bannon could not allow Canberra’s reform agenda to overshadow the states’ fiscal problems. To fix the situation, Bannon said, “I strongly urge you to recognise the need for a better ongoing relationship between the States and the Commonwealth”. Hawke’s call to expand the Premiers’ Conference to include microeconomic reform would be acceptable to the states if the Commonwealth would “act responsibly in providing appropriate financial assistance to the States”.¹⁰⁹ Hawke even presaged that a special Premiers’ Conference could be held later in the year to concentrate on microeconomic reform (Hancock, 2013). All of the key elements of a ‘closer partnership’ were ready to be picked up. Instead, competitive federalism showed its ugly side.

At the June 1990 Premiers’ Conference, Premiers were not informed of the Commonwealth’s bargaining position until 7:30am the day of the conference, when the document was slipped under the hotel door. Premiers, Ministers, and state officials had three hours to digest the deal and prepare a response. Then in the actual negotiations, the Commonwealth presented its position as *fait accompli*. Worse still, the Commonwealth’s deal

¹⁰⁷ JBC, Folder: Premiers Conference 28/06/1990 (2), “Statement by the Treasurer, the Hon P.J. Keating MP – Economic Context of the Premiers’ Conference,” 27 June 1990, p.6.

¹⁰⁸ JBC, Folder: Premiers’ Conference 28/06/1990 (4), “Letter from Greiner to Hawke,” 14 June 1990, p.1.

¹⁰⁹ JBC, Folder: Premiers’ Conference 28/06/1990 (3), “Letter from Bannon to Hawke,” 20 June 1990, p.6.

was considered to be “horrendous” by Bannon. He then led the Premiers in “an unprecedented revolt against a federal proposal to slash their funds by \$400 million...The Premiers’ Conference, reportedly marked by a series of fiery clashes, is believed to have broken up with the abrupt exit of the PM, Mr Hawke”.¹¹⁰ For the first time in 20 years, the Premiers had forced a second day of negotiations, at which time the Premiers “established a good rapport” with each other in opposing the Commonwealth’s dominance (Hancock, 2013, p. 254). This was helped by the fact the decision to actively resist Canberra’s offer “emerged out of a number of meetings between the States before the conference started and during the early part of it” (Cain, 1995, p. 170). Premiers did not meet separately according to political party; it was noted a Labor-only Premiers’ meeting before the conference was unacceptable. Not only were political optics a concern but the size and importance of NSW trumped partisanship between the Labor Premiers and NSW’s Liberal Premier.¹¹¹

The process was so frustrating and destructive towards Commonwealth-state relations that afterward even Hawke was embarrassed.¹¹² The 1990 Premiers’ Conference demonstrated to Cain that premiers’ conferences were no longer conferences but “a monologue by the Commonwealth in the form of an offer document...and a ‘take it or leave it’ attitude” (Cain, 1995, p. 170). “The conventions of warfare took precedence” to the special relationship on microeconomic reform that Hawke was trying to develop with his closest ally, Premier Greiner (Hancock, 2013). Greiner’s government produced a report indicating that microeconomic

¹¹⁰ JBC, Folder: Premiers’ Conference 28/06/1990 (1), “News clipping: ‘Premiers in Revolt, Bannon leads charge against \$400m cutback,’” June 1990.

¹¹¹ JBC, Folder: Premiers Conference 28/06/1990 (1), “Notes of Meeting between the Premier and the Federal Treasurer Paul Keating,” 4 May 1990.

¹¹² Interview with former senior state government official, 11 June 2014.

reform, eliminating service overlaps and duplications, and reforming fiscal relations could contribute to Hawke's effort to internationalize the Australian economy (*ibid*). Yet what was needed to see this effort through was cooperative IGR. Coincidentally, Bannon issued a statement prior to the 1990 Premiers' Conference in which he stated that "with the co-operation of all parties, this meeting could be a watershed in the history of Commonwealth-State financial relationships".¹¹³ The policy community was also coming around to this conclusion as they responded to the slow pace of change (Carroll, 1995). Even after COAG was founded, EPAC reported that continued cooperation between the orders of government was necessary if microeconomic reforms were to realize their full potential (Dao et al., 1993).

The transformation of the Australian economy was a central plank of Hawke's objectives, which he believed would lead to economic recovery and lasting prosperity. Yet when attempting an ambitious microeconomic reform effort, Canberra was constrained, as all federal governments are, by the constitution's division of power between centre and sub-units. In a speech to the NPC on 11 May 1988, SA Premier John Bannon spoke exactly to this point: "To attempt reform when the majority of the state governments are in disagreement is a truly daunting task even for a PM possessing Whitlam's persuasive powers".¹¹⁴ Commonwealth-only reforms to the macro-economy and tariff rates could only achieve partial gains; they had to be accompanied by deeper reforms. With the states having power over significant policy areas that required modernization, Hawke had no choice but to enlist the states on all fronts in order to

¹¹³ JBC, Folder: Premiers' Conference 28/6/1990 (2), "News Release: State Premiers Agree to Package for Premiers' Conference," 26 June 1990.

¹¹⁴ NLA, Speech by John Bannon at the National Press Club, 11 May 1988, nla.obj-222524299.

complete Australia's transformation into an internationally competitive economy. The 1990 Premiers' Conference dust-up seemingly ended any chance at cooperation.

In the end, Hawke managed to save his reform agenda with his leadership. He altered the Commonwealth's tack and agreed to a 'closer partnership' not just on microeconomic reform but on almost everything else, including fiscal arrangements. The idea to reform the IGR system originated from Mike Codd, Head of the Department of Prime Minister and Cabinet (DPMC): "Codd had been unable to snag the interest of [former PMs] John Gorton, Bill McMahon, Gough Whitlam or Malcolm Fraser". He tried again with Hawke after the 1987 election but the time was not ripe, according to Hawke. After the 1990 election, Hawke was reported to have said "Right. We're going to do this!" (D'Alpuget, 2010, p. 317). Reconciliation had been a central theme of Hawke's prime ministership since the National Economic Summit. The disastrous Premiers' Conference in June 1990 no doubt helped to turn his attention towards reconciling with the states.

As a former union leader, cooperation and consensus were central elements of Hawke's decision-making. Yet he also thrived on conflict: "he was happier and more successful as a troubleshooter called in at the eleventh hour to resolve some crippling dispute than as an administrator caught up in the daily organisational grind" (Anson, 1991, p. 2). The 1990 Premiers' Conference dust-up and the ongoing recession certainly required a trouble-shooter to bring all the parties together to launch a concerted reform agenda. Even prior to 1990, Hawke and Keating recognized that fundamental reforms were necessary if Australia was to avoid the curse of being a 'lucky country'. Keating is largely seen as the architect of these macro-economic reforms, with

Hawke as the salesperson,¹¹⁵ attempting to overcome the public's skepticism (a characteristic Horne had recognized decades early). Hawke also understood the broader transformative affect these reforms would have on all aspects of Australian life: "Australia stands poised on the threshold of the 1980s more divided within itself, more uncertain of its future, more prone to internal conflict, than at any period in its history" (ibid., p. 67).

It helped that Hawke's extraordinary political success was due to his "love affair" with the Australian people (Mills, 1993). He may not have crafted the transformation's details, but he did lead a skeptical country down the road of reform and they followed him with four successive electoral victories. No doubt he was also concerned about his legacy when he began the seemingly impossible task of reforming the Australian federal system. He was a politician that was "never satisfied with ordinary achievements, or even with extraordinary achievements if they were secured by ordinary means" (Anson, 1991, p. 4). He also pragmatically accepted things as they were, and he did so with a "complete and unflagging belief in the power of negotiation" (Mills, 1993, p. 10). In the Australian context, reforming federalism was a fool's errand. Yet when a window of opportunity presented itself, Hawke the co-operator, pragmatist, negotiator, charmer, and fighter, boldly stepped through. In order to salvage his reform effort, Hawke arrived at the NPC in July 1990 and delivered his 'Closer Partnership' speech on new federalism, declaring that the Commonwealth needed the states and that he was personally ready to reset the relationship with them. But were the states inclined to join him?

¹¹⁵ See J. Edwards (1996). According to Anson (1991, p. 150), "Hawke thinks he is the government, Keating thinks he does the governing".

Conclusion

Despite Australia's higher VFI, more integrated party system, and constitutionally-assigned policy concurrencies, the Commonwealth and states still engaged in competitive federalism. Cooperative federalism – in terms of the routinization and value infusion of IGR institutions – was weakly institutionalized up to and including the 1990 Premier's Conference, which acted as a critical juncture for Hawke's 'Closer Partnership' speech. At that time, a window of opportunity opened during which IGR institutional change seemed possible, not because of these independent factors but despite them. Prior studies acknowledge all these factors but no study has analyzed them to produce a comprehensive narrative that considers each factor and elaborates on the impact of the mechanism of continuous negotiation on Australian IGR.

The chapter has demonstrated that cooperative federalism in Australia required further inducements before it found expression. The full story cannot be told without appealing to the political economy. Hawke's 'closer partnership' proposal was as much a reaction to shifting external economic realities as it was a personal expression of leadership and a recognition of the fiscal and policy interdependencies that existed between the orders of government. Throughout their first three terms, Hawke and Keating sought to unilaterally change the Australian economy from Canberra. Their reforms and fiscal restraint unleashed further demands for reform at a time when Australia's external market integration was rapidly diffusing. The 'turn to Asia' and a lagging Australian economy pushed Hawke to commit to a broadly-based reform process with the states, thus engaging the mechanism. After 1990, he and the Premiers learned very quickly about competitive federalism's inability to address the multi-faceted problem they all encountered. Completing both the fiscal reforms – to handle severe deficits – and the

microeconomic reforms – to handle policy duplication and overlap as well as the economy's adaptation to liberalization and internationalization – required a 'new federalism' initiative. The next chapter demonstrates how the political economy variable played a key role during continuous negotiations to acquire actors' commitment to economic reforms and to expand the discussions to include IGR institutional reforms.

Chapter 4:

Why 'Closer Partnership' led to COAG

[The SPC process] has the capacity to be the most significant period of reform in the 90 years of Australian history.¹¹⁶

Nicholas Frank Hugo (Nick) Greiner
Premier of New South Wales, 1988-1992

¹¹⁶ NLA, Speech by Nick Greiner at the Special Premiers' Conference, Brisbane, 30 October 1990, Npf 354.9400725 S741, p.3.

The following continues the analysis of COAG's institutionalization. PM Bob Hawke promised in the 1990 election campaign to continue with economic reform but there was no mention of a 'new federalism' initiative. Despite the Commonwealth's many reforms, the economy remained weak. Reform begat further reform across all policy fields, which was the only way to address the 'lucky country' challenge. Some of those policy fields included microeconomic reform, which the states controlled by virtue of their powers under the Constitution. If Australia was to take advantage of the 'turn to Asia', then Hawke needed the states' cooperation. But as the events at the 1990 Premiers' Conference demonstrate, this was neither guaranteed nor easy. Why did the states accede to Hawke's request for a new and 'closer partnership'? The following chapter demonstrates that their economic and fiscal circumstances, and political leadership, provide an explanation.

Regarding the economy, it was clear that, by the late-1980s, the Commonwealth's macro-economic reforms were impacting Australia's regional economies, which affected state politics.¹¹⁷ As a result, Australia's IGR system was directly exposed to external pressures. The dust-up at the 1990 Premiers' Conference was a clear sign of stress. The following shows that actors confronted a stunning reality: both orders of government were incapable of independently managing Australia's internationalization. The SPCs were launched on this basis.

Regarding leadership, the following demonstrates that state politics also produced leaders who were open to new ways of operating the IGR system. They were encouraged by SA Premier Bannon, also at the time National President of the Australian Labor Party, who championed the cause of reform long before any changes were actually implemented. And they

¹¹⁷ See Walsh (1993).

were shown the light by Premier Greiner's non-partisanship and aggressive reform programme. Leading by example whilst wielding the political capital of Australia's largest state helped bring the rest of the states to the table.

Once the state positions are elucidated, the chapter follows the SPC process to its conclusion, the founding of COAG. It demonstrates that the mechanism of continuous negotiation was able to expand the economic reform negotiations to include discussions on IGR institutional reform because of an incentive to cooperate emanating from the political economy of Australia and the states. Whereas Hawke started the SPC process, it was the states that eventually forced it to a successful conclusion.

The View from the States

On 25 July 1990, Hawke's call for a 'closer partnership' was taken up in a speech at the NPC delivered by Nick Greiner, Premier of NSW, the largest and most important economy within Australia. At the time, NSW also had the only state government on the continent controlled by Labor's political opposition, the Liberals. Even though Greiner's speech on microeconomic reform was scheduled before Hawke delivered his speech, "[Greiner] seized the moment...to give what in essence became the States' response to Hawke's 'New Federalism'" (Hancock, 2013, p. 256).¹¹⁸ Rather than oppose Labor, Greiner laid out a path to cooperation in stark contrast to explanations of cooperative federalism that rely on partisanship and an integrated party system.

Greiner immediately started his speech by calling upon all Australian governments to take up the challenge already accepted by unions and employers: "they must restructure if Australia

¹¹⁸ Sturgess (1992) concurs.

is to compete internationally”.¹¹⁹ To achieve that goal, Greiner shared the PM’s vision for a “historic restructuring of Australian government”. Greiner’s government and some of the other state governments already had a record of reform by the time Hawke sought major microeconomic reform. Why did Greiner and the others undertake such a program and why was a Liberal Premier agreeing with a Labor Prime Minister? Greiner’s reasons were 1) recent moves in the EU to remove trade barriers; 2) growing demands for international competitiveness; 3) reform minded PM and Premiers; and 4) the Australian federation’s centenary. The first and second reasons helped to perpetuate the economic reform process described in the preceding chapter; world economic shifts were washing up on Australia’s shores and Australians had to respond, hence Greiner’s third reason.

Regarding the fourth reason, both Greiner, Bannon, and others stated that the 100th anniversary of federation in 2001 – as well as the 1988 bicentenary celebrations of the landing of the First Fleet in Australia – seemed to capture the imagination of politicians and citizens, turning their attention to matters of national importance; Australia was coming of age. As one former politician described it, “we were thinking about how far we’ve come,” which provoked thoughts about the national interest. He continued, “there was a recognition by those driving the reforms to think about the future, to think Australia first, [one’s own state] second...There was a belief that as a nation we had to reach out instead of fighting each other”.¹²⁰ By focusing on issues of national scope, it was easier for politicians from both orders of government to advocate a process of reform that could overcome the usual partisanship and get on with the task at hand.

¹¹⁹ NLA, Speech by Nick Greiner at the National Press Club, 25 July 1990, nla.obj-222571923.

¹²⁰ Interview with former senior state government official, 19 June 2014.

Accepting the PM's call for a series of SPCs became politically acceptable to voters and paralleled the Premiers' own reform agenda.

Besides being in tune with the current political mantra, reform was necessary to deal with the 1990-1 recession and Australia's decreasing competitiveness. Former officials described changes in the international economy as one reason for why HoG cooperated: "There were no longer any guarantees from Australia's traditional buyers" of agricultural goods, particularly with the EU's common agriculture policy. Unlike in Canada, Australia in the 20th century did not have a guaranteed trade partner. Japan's transformation into a manufacturing superpower was also shifting attention to Asia: "It began to be recognized that to survive, Australia needed to look to Asia....Part of [Asia's] success is their wage structure, which is low compared to Australia. This was a big factor in focusing on the national interest". Instead of competing to service the Asian market, "the national strategy stopped states competing and started them working together to take advantage of Asia more effectively".¹²¹ Taking advantage meant adjusting to a tariff-free marketplace, which Australia's manufacturing sector was ill-equipped to handle without significant structural reforms from both orders of government.

One way to effect reform was via the SPC process, which was, according to Greiner, "an opportunity for genuine reform and an achievable framework".¹²² If the Commonwealth needed the states to achieve microeconomic reform, then the states needed the Commonwealth to fund the implementation of those reforms. Indeed, states tend to emphasize their share of the costs of reform rather than acknowledge the potential nation-wide benefits (Industry Commission,

¹²¹ Ibid.

¹²² NLA, Greiner at NPC, 25 July 1990.

1994, p. 56). An example is the problem of duplication, which was key to the entire reform effort. As Hawke stated in his 'Closer Partnership' speech, duplication was inefficient and costly. Yet as Fletcher (1991) points out, overlap and duplication of services are either cost inefficiencies or signs of a responsive, democratic federal system. Responsive policy-making is a direct result of governments attempting to service the same population. Duplication occurs when they 'bump' into one another. Therefore, completely eliminating duplication and overlap is not possible nor desirable.

Nevertheless, both Hawke and the states pointed to the need to deal with the issue. Their agreement that the problem existed and needed reform was an important factor in launching the SPC process. At times however, overlap and duplication were synonymous either with Commonwealth government activities that the states wanted to curtail or with the Commonwealth's supervision of the states' implementation of federal policies. The SPC process was designed to place the Commonwealth and states on an equal footing in order to examine the problem without prejudice. Greiner's response to Hawke indicated that the states were ready to engage with the Commonwealth if it "substantially moderate[d] the arrogance which marks most of its dealing with states. There is now a wealth of talent in state administrations such that a devolution of responsibility would cause no weakening of program control." He also asked that the Commonwealth be "fair" with its redistributions to the states upon agreeing to functional redistributions.¹²³ In this way, the states and Commonwealth could move beyond the cost and financing issues and achieve real reform.

¹²³ Ibid.

According to Greiner, dealing with duplication and overlap would solve “the tragedy that Australian international reputation should have been so damaged because of a failure by the states to agree on a strong and well-resourced national company regulator”.¹²⁴ In other words, the reform effort was too important for politicians to use it to score partisan political points against other parties or orders of government. Fixing the duplication and overlap problem required both orders of government to critically re-examine their relations with each other. The point regarding partisanship is also significant since Greiner was the only Liberal HoG at the time of his speech, notwithstanding the NT and ACT Chief Ministers. Partisan attacks pitting him against the Labor PM or Premiers would have scuttled the entire reform process. There were no guarantees. For decades, economic development was the universal theme of state partisan politics (Galligan, 1986). Why would the Premiers cast aside their partisan political purposes, especially considering Australian’s penchant for state welfare?

Indeed, one counter argument for the emergence and subsequent success of the SPCs and institutionalization of COAG is that almost all the HoG were from the Labor Party. Therefore, it was easier for them to get along and agree on a reform programme. The importance of party in Australia cannot be overstated: “Placed in a comparative perspective, the hallmark of Australian politics is the dominance of party” (McAllister, 2002, p. 380). Since most voters identify with one party or the other, it can be argued that when federal and state parties are engaged in IGR, a sizable coalition of voters is carried with them. This grants party leaders significant leeway and influence. Australian parties are also part of system “which exists solely to maximize

¹²⁴ Ibid.

efficiency” (ibid., p. 381). Getting results is paramount and if all of the leaders were from Labor, they could prove the Party’s ability to govern over and above their Liberal opponents.

Political parties were seen as contributing to successful IGR. In 1988, Bannon referred to the absence of destabilizing pressure “largely as a result of the ascendancy of cooperative Labor states”.¹²⁵ It suggests that a sole Liberal HoG was forced to go along with the Labor majority or else fight a battle against his/her fellow states *and* Canberra in which a lack of results or the impression of such could spell trouble at the polls. In actuality, Greiner was one of the key leaders of the reform effort and it was his influence that brought reluctant Labor Premiers to the table.

WA Premier Lawrence alluded to a lack of partisanship by 1990 when she discussed the emergence of a consensus for change. In a speech at the NPC to respond to the launching of a state inquiry into corruption, Lawrence outlined how respect towards Australian politics and politicians could be restored. One way was to end the traditional posturing between the Commonwealth and states, since “the mileage for state leaders in Canberra-bashing...is diminishing”. Rapprochement between the Commonwealth and states was occurring because “our political divisions, I believe, are narrowing with the pressure of international forces on our economy. I believe a consensus has emerged for far reaching change”.¹²⁶ In other words, the traditionally conflictual parties and governments were now finding themselves agreeing on a crisis context because of external pressures. Bannon stated that “pragmatic cooperation has been shown to achieve much in a climate where the economy has been under stress”.¹²⁷ Analysts

¹²⁵ NLA, Bannon at NPC, 11 May 1988, p.6.

¹²⁶ NLA, Lawrence at NPC, 27 June 1990.

¹²⁷ NLA, Bannon at NPC, 11 May 1988, p.12.

of Australian parties also reported that it was becoming increasingly difficult to differentiate the federalist leanings of the two parties.¹²⁸

Rather than encourage cooperation, sometimes partisanship and personalities combine to product conflict and competition. Referring directly to Bannon's assertion that Hawke did not face destabilizing pressure from Labor governments, it must also be noted that this same lack of pressure did not produce constructive and effective Premiers' Conferences. According to Victorian Labor Premier Cain, the 1990 Premiers' Conference was not even the high water mark for the Commonwealth "playing tough with the States"; this happened with the 1988 budget and its surprise A\$1.5 billion in cuts (Cain, 1995, p. 166). As Bannon discusses, even though the states helped the Commonwealth see through its financial reforms and austerity measures through to 1988, that states had no choice but to accept the Commonwealth's position. Financial regulation is the purview of the Commonwealth under the constitution, as is the collection of taxes, which the Commonwealth largely distributes as it sees fit. Therefore, faced with spiralling deficits and interest rates, the Labor Premiers had no choice but to accept cuts. It is plausible they were amenable to the cuts being handed down by a fellow Labor HoG but in the end, faced with continuing cuts and little consultation, the states eventually did not go quietly.

One reason for the split was because "any comparison of the branches of the Labor Party suggests that it is more appropriate to talk of nine distinct parties" (Jaensch, 1989, p. 121). At one point, Keating "complained that Bannon's criticisms of the Commonwealth on behalf of all Premiers were 'politically damaging to the Labor Party'" (Parkin & Marshall, 1992, p. 114). Cain

¹²⁸ See Hollander and Patapan (2007, p. 284). Labor traditionally was anti-federal, to the point of actively seeking to abolish the states.

remembered “[saying] to Bob and Paul, ‘You are seen by genuine Labor people as not caring about our people’They were unmoved,” he recalled (Cain, 1995, p. 165). Being from the same party may have helped in some ways, but it does not explain why Commonwealth-state relations turned so quickly from competitive to cooperative in the early-1990s. If it was because a majority of HoG were from the Labor Party, then why did relations not change during the other eras of one-party dominance of Australia’s governments?

The effect of partisanship was diminished partly because, after being bullied around enough times by the Commonwealth, Premiers forged strong links between themselves regardless of their party affiliations. When Greiner ousted a thirteen-year long Labor regime in NSW, he quickly joined his fellow Premiers in resisting the Commonwealth’s tactics even though there were sound economic reasons for Canberra’s policies. Therefore, “[the SPCs] were not divided on party lines. There is a mixture between parties and sometimes cooperation is greater across party lines because both recognize they are working in the national interest”.¹²⁹ Thus, there were other factors at work that encouraged the states to cooperate.

The following examines the states and investigates their reasons for agreeing to a ‘closer partnership’. Whilst the exact reasons are numerous owing to their different economic and political circumstances, each state experienced troubling economic conditions that forced reforms one way or the other. As Galligan (1986, p. 254) pronounced, “state politics is parasitic on...economic conditions”.

¹²⁹ Interview with former senior state government official, 22 July 2014.

South Australia: leading the way

During John Bannon's decade in office beginning in 1982, he accurately diagnosed the major issues and problems facing Australia. For most of his tenure, the states were faced with the direct consequences of recession and austerity. Bannon's approach was to govern cautiously because "it was increasingly apparent that South Australia was vulnerable to national and international economic trends, and that careful attention to the State's economic structure would be required" (Parkin, 1992, p. 10). Bannon focused his attention primarily on the problem of service overlap and duplication between the orders of government. His call to Hawke personally and to all the other HoG at the 1986 Premiers' Conference for a major review of the issue went unheeded despite his assertion that "there is scope for very substantial real savings" (Parkin, 1996b, p. 99). Nevertheless, EPAC began to investigate the potential savings from functional reallocation of governments' responsibilities.

Meanwhile, by the time the Commonwealth began implementing austerity measures in the late-1980s, Bannon had successfully reduced debt per capita to half that of neighboring Victoria (Parkin, 1992, p. 15). Both Vic and SA are two of Australia's leading manufacturing states. In particular, SA was home to a large portion of Australian car and 'white goods' manufacturing as a result of state-led industrialization between the 1930s and 1960s.¹³⁰ SA also relies relatively heavily on agriculture, largely due to lower levels of mining and construction activity (G. M. Scott, 1992). Its economic structure means that SA acts as a leading indicator of the health of the Australian economy.¹³¹

¹³⁰ See Parkin and Jaensch (1986); G. M. Scott (1992).

¹³¹ "...with an industrial structure fairly similar to that of Australia as a whole" (The Treasury, 1990). See also Parkin and Jaensch (1986).

Bannon's 'good housekeeping' strategy of incremental change and careful management were not enough, however, to prevent further economic decline. SA recorded the highest unemployment in the country during the 1990-1 recession. Indeed, SA experienced unemployment above the national average for all of Bannon's tenure in office (G. M. Scott, 1992). Reduced transfers from Canberra affected SA's ability to manage the problem. The state government calculated that the Commonwealth had reduced transfers to the states by 14% between 1986 and 1992 even as it increased its own spending by 6.2% (Parkin, 1996b). Tax and fee increases were of little help. SA's deficit increased overall from A\$96 million in 1982 to A\$500 million in 1992 (G. M. Scott, 1992).¹³²

Bannon's careful balancing of economic, environmental, and social justice issues was unable to right the economy. SA's difficulties forced Bannon to publicly repudiate the Commonwealth's policy of high interest rates, which were designed to curb imports and reduce the current account deficit (Parkin, 1992). Whilst others states were experiencing the beginnings of an investment boom in the late-1980s, SA was unable to "just sit back and reap these energy and mineral riches; that was clearly wrong".¹³³

The result was that SA was one of the first states to push for microeconomic reforms aimed at cost-savings, in particular calling for a national electricity grid. Such a grid would reduce management costs and increase efficiency and reliability, thereby delivering costs savings to businesses, consumers, and state governments: "We took the initiative on that; we argued it through and, indeed, it was our...opening up of the issue that I think has made this talk of a

¹³² The 1992 figure was adjusted to remove the one-time State Bank bailout package.

¹³³ State Library of South Australia, Adelaide (herein Adelaide), Mortlock Library of South Australia, J.D. Somerville Oral History Collection, OH89/40, "Interview with John Charles Bannon," 20 October 1992, p.1.

national grid possible”.¹³⁴ These kinds of reforms were very important since state government stimulus directed towards economic development was generally regarded as ineffective: “Any State government is inhibited from operating an independent economic policy by the ‘openness’ of the State economies” (G. M. Scott, 1992, p. 83).¹³⁵ In other words, SA could not compete with the larger states (nor with Queensland’s weather!). SA’s economy was one of the few to rely more heavily on inter-state than on international trade, particularly the export of manufactured goods (The Treasury, 1990). Therefore, microeconomic reform of the Australian economy was paramount to South Australia.

In response the government commissioned the Little Report, which advocated for reform that would restructure the SA economy away from manufacturing and towards Asia (Parkin, 1992). The Report was blunt: “SA’s economy is poorly structured and vulnerable” (Arthur D. Little, 1992, p. i). Manufacturing had for too long relied upon tariffs. The Garnaut Report’s recommendation for the complete and immediate elimination of tariffs would expose the fact SA “has an outmoded industrial structure that is ill-suited to competition in global markets” (ibid.). SA’s future growth required an advanced manufacturing sector that could compete on the basis of quality, service, speed, and perception. As well, “South Australian firms must accept that their ‘domestic market’ has been redefined to include Asia-Pacific as a whole” (ibid., p. xvi). The Report noted that in comparison to similar sub-units in other federations – such as Manitoba, Saskatchewan, New Brunswick, and Schleswig-Holstein – SA had the smallest amount of exports as a percentage of GDP (ibid., p. 2). Australia was in generally poor shape; it came second to last

¹³⁴ Ibid., p.7.

¹³⁵ Also, “it is only in regard to particular project or institutions that a State government has room to manoeuvre” (G. M. Scott, 1992, p. 71).

in a comparison of 22 OECD countries on economic internationalization (ibid., p. 10). Catching up required better links with Asia, export development incentives and assistance, an investment attraction strategy, a strong business climate, public service reform, and a refocused education system. Achieving these goals required microeconomic reform.

Thus, when Hawke called for a 'closer partnership' to transform the Australian economy, he found an ally in John Bannon. Bannon described Hawke's proposal as a "desire for a landmark reform in his fourth term" (Parkin, 1996b, p. 100). But Bannon deserves credit for being a first-mover on economic and IGR reforms. He was advocating for IGR reform for almost a decade as part of his efforts to transform SA's economy¹³⁶ and he was vindicated on his contention that overlap and duplication were major problems. Coincidentally, EPAC's support of his contention was released on the day of Hawke's 'Closer Partnership' speech (Parkin & Marshall, 1992).

The conclusion that "the Bannon decade was not one where substantial economic progress was made" (G. M. Scott, 1992, p. 97) is not necessarily a sign of failure on Bannon's part,¹³⁷ particularly when viewed alongside his debt containment effort,¹³⁸ recognition of major problems within the federal system, and the fact that SA's public sector "is more economical, often more oriented towards the needs of those it serves and frequently more efficient than it was ten years before" (Radbone, 1992, p. 101). More rather, the economic situation in Australia's leading indicator state – and Bannon's attempts at reform – highlighted the fact that a coordinated and cooperative approach to reform was needed to change Australia's economic

¹³⁶ Some success was found in the minerals and energy sector, where the Bannon government "sought greater cooperation and coordination between the public and private sectors and between all governments [in] securing longer term oil and gas supplies at guaranteed prices and the development of national gas and electricity interconnections" (O'Neil, 1992, p. 194).

¹³⁷ Although his cautious, managerial style received criticism, see Patience (1992).

¹³⁸ Real debt per capita was below 1982 figures before the 1991 State Bank bailout (\$3078 compared to \$3499).

fortunes. Adapting to changing economic conditions required a whole-of-country approach to reform. Despite its best efforts, SA on its own could not right itself:

The State economy has been particularly vulnerable to the decline of 'rustbelt' industries, to reductions in tariff protection, to the vicissitudes of drought and to the vagaries of agricultural export prices...[It is] distant from the dynamic resource-based economies in WA and QLD, from the major commercial and population centres of Sydney and Melbourne, and from the Asia-Pacific region widely perceived as the appropriate focus for Australia's economic future" (Parkin, 1996a, p. 15).

Addressing these issues was a challenge for all Australian governments; a closer partnership of some kind between them was needed.

New South Wales: committed reform partner

Bannon's recognition of a pressing need for economic and IGR reforms would not have found expression without the support of NSW's Liberal Premier, Nick Greiner. NSW's position as the largest state, by GDP and population, means that the opinion of its government matters. In terms of Hawke's proposal for a 'closer partnership,' what really mattered to Greiner was policy, for he too recognized early on that microeconomic and VFI reforms were crucial to Australia's economic future.

When in opposition between 1983 and 1988, Greiner was astounded that NSW had "the most diversified and well balanced regional economy in Australia,...has a large, highly educated population...But the State is not living up to its potential" (Sturgess, 1992, p. 28). According to Greiner, righting the situation required two essential elements: encouraging a climate of entrepreneurship, which included removing red tape and wasteful subsidies as well as deregulating or crafting better quality regulation, and creating a "more responsive, more accountable and better managed public sector" (ibid., p. 28), which included small changes, like

phasing out the government-run office cleaning service, for example, and much larger reforms, such as to the electricity market. These reforms, his advisers believed, “really are in the best interests of the middle sort of people” (ibid., p. 39).

His views went beyond mere policies and included contemplating modern democracy itself. Politicians, he said, were “becom[ing] isolated from the people” due to interest-group politics and their reliance on lobbyists (ibid., p. 46). He believed this dynamic forgot the public interest. Greiner understood that the Liberal Party’s future lay “in a genuine attempt to govern in the long term interest of all the people. If we do not, the consequences for Australia are most serious” (ibid., p. 37) as more time and energy are taken up seeking rents from government rather than fostering entrepreneurship.¹³⁹ The fairness of Liberal Party policies would expand their voter base, which included establishing a dialogue with unions (ibid.). He even repudiated his own party’s blind adherence to the notion of state’s rights (Hancock, 2013, p. 247). Rather than rely on party integration to dictate intergovernmental cooperation, Greiner established his own pragmatism on governing, one that allowed him to accept Hawke’s ‘closer partnership’ when it was proposed in 1990. It helped that his thinking was not ‘New Right’ philosophy: “he was uncomfortable with the notion of ‘deregulation’; the aim was for less and better regulation” (ibid., p. 146). Greinerism was not Thatcher- or Reagan-ism. Greiner embraced a notion of Australian liberalism as practical and anti-ideological (ibid., p. 148). Greiner praised Hawke for his “modesty about the capacity of government” (Sturges, 1992, p. 59) and thought “Australian Governments need to be getting back to basics” (ibid., p. 63).

¹³⁹ Greiner’s senior advisor, Gary Sturges, understood the public interest issue from the perspective of the collective action problem, see Sturges (1992, p. 217).

To implement his philosophy and ideas, Greiner first had to be elected Premier. Labor had run NSW since 1979 and it was time for change: “there is a feeling of old age and a loss of direction in the Labor government” (E. Thompson, Painter, Wheelwright, & Mutch, 1986, p. 5). Yet long-running governments are not always easy to defeat. Greiner and his Liberals needed an issue to galvanize the electorate. His strategy of focusing on corruption opened the door to a no-nonsense, get-down-to-business premiership that was ready to enact significant changes. Laffin and Painter (1995b) argue that the impetus for reform came from several sources. For one, the external economic environment and NSW’s deficit certainly forced change. Hawke and Keating’s reforms had opened up the Australian economy and the effects were being felt at the local level. From Greiner’s perspective, “Keating and Hawke did not deregulate the capital markets as an act of ‘visionary leadership’ but out of necessity – they were ‘mugged by reality’” (Laffin & Painter, 1995b, p. 7).

Greiner’s advisers were also being informed by events in New Zealand (Hancock, 2013, p. 208).¹⁴⁰ In the mid-1980s, NZ was focused on the same sort of microeconomic reforms that Australia would consider almost a decade later. NZ was pressured into reform by its fiscal position and extreme exposure to world economic fluctuations. Its Labour Party under PM David Lange was responsible for implementing change, ending interventionist policies (the last of which were PM Robert Muldoon’s ‘Think Big’ strategy) and “more fully [grounding NZ] in a reality that we were in denial about for far too long” (Johansson, 2005, p. 219).¹⁴¹ Like Australia, NZ was faced with declining terms of trade and responded by liberalizing its financial system, reducing tariffs,

¹⁴⁰ See also Sturgess (1992).

¹⁴¹ See also Holland and Boston (1990).

and ending subsidies. With close ties between the two countries – including a free trade agreement¹⁴² – policies on internationalization and liberalization diffused to Australia.

Once Greiner closed his desk drawer on the election, he opened his drawer on governing.¹⁴³ According to Greiner, the drawer was not full of ideology or interest groups or partisanship but of “common sense...courage and leadership...If you continue losing half a billion dollars on railways and so forth, the place would go backwards” (Laffin & Painter, 1995b, p. 9). According to Hancock (2013, p. xi), Greiner’s “emphasis on evidence-based, rational approaches to decision-making; the ready acceptance of change and risk; the focus on outcomes rather than processes; the preference for practical solutions over ideological consistency” originated or were reinforced during his time at Harvard Business School. The result was a zeal for reform that saw Greiner “set a frenetic pace” in the first days of his term (ibid., p. 193), which stood in contrast to Labor’s penchant for “moderate changes” (E. Thompson et al., 1986, p. 22).

Convincing voters that major reform was needed and needed quickly was handed over to the Curran Commission of Audit. Its central message of severe budget problems paved the way for restructuring: “Debt reduction became the overriding justification for service cuts, job cuts and asset sales” (Laffin & Painter, 1995b, p. 10). With the Curran Report acting as an “agent of reform”, Greiner justified further changes (Hancock, 2013, p. 207). These were based on a post-bureaucratic model, whereby government is viewed as a “pattern of politically tightly controlled small, policy-focused ‘core’ departments supervising decentralized, mission-centre

¹⁴² See NLA, Speech by Bob Hawke at Parliamentary Dinner for NZ PM Geoffrey Palmer, 2 July 1990 (see also <https://pmtranscripts.dpmc.gov.au/release/transcript-8048>). The agreement is referred to as Closer Economic Relations.

¹⁴³ “I literally had a drawer for elections and a drawer for government” (Laffin & Painter, 1995b, p. 7).

organisations...which are driven...by competition and customer expectations” (Laffin & Painter, 1995b). Once the government was restructured along these lines, microeconomic reform of the economy followed. Examples included deregulating egg production, commercializing waterworks, and closing rural railways. A major element of Greiner’s microeconomic reform agenda was corporatisation, whereby government-controlled enterprises operate according to market rules yet are held in a public trust. Examples included the railways, electricity commission, and grain handling (Greiner, 1990).

None of these reforms would have succeeded if not for the fact that many in the bureaucracy agreed with Greiner’s vision for modernization.¹⁴⁴ His policies were constructed not from public opinion but from his common sense attitude, which was evident in his razor-thin re-election in May 1991 when the Labor opposition won the popular vote but did not obtain a majority of seats. His almost blasé attitude towards the political consequences of reform “alarmed Treasury officers” but nevertheless impressed them and encouraged them to work on reforms (Hancock, 2013, p. 197).

Greiner and his advisors were operating at a time when microeconomic reform of the Australian economy was in its infancy and had not caught on nationally or in most of the other states (Painter, 1995b). When Hawke announced his ‘closer partnership’ proposal, Greiner’s team viewed it as “an ideal setting where ‘statesmanship’, ‘leadership’, the ‘politics of commitment’ and the rhetoric of hard-headed economic argument could hold sway” (Laffin & Painter, 1995b, p. 11). The SPC agenda was an opportunity for Greiner’s common sense, pragmatic reform agenda to find expression on the national stage. Sturgess (1992, pp. 147, 152)

¹⁴⁴ See Laffin and Painter (1995b).

had only just complained in April 1990 that NSW's reform programme was give "too little recognition." He called for the Commonwealth to set the agenda and to review the financial reforms that would determine the pace of the microeconomic reforms, especially since competition policy reform at the state level were being curtailed by the VFI (P. J. Forsyth, 1995). Sturgess's pessimism about the pace of reform was later replaced by an understanding that "most of the States...[had] embraced a bolder program of reform since September 1990, partly through the process of the SPC" (Sturgess, 1992, p. 199). The fact that it was a Labor PM setting the agenda was of no consequence. Greiner was post-ideological, practical, and not interested in scoring "political points, for what he saw to be economically rational outcomes" (Laffin & Painter, 1995b, p. 13); he "considered himself 'knowingly' indifferent' to the politics of any given situation" (Hancock, 2013, p. 219). Greiner continued, "Bob [Hawke] was not the normal, centralist Labor PM, but interested in a workable compromise. Most of the Labor premiers would go along with, if I did. So there was a unique opportunity for reform" (D'Alpuget, 2010, p. 318).

Greiner played the part of any state Premier – complaining about Canberra's control of finances and blaming it for tax rises and service cuts – but the Hawke-Greiner relationship eventually overcame the yearly showdown at the Premiers' Conferences and typical partisan rhetoric. Both agreed on the need for a fundamental restructuring of the Australian economy and both sought to address the VFI. Once the SPCs were underway, economic and financial reform led them to consider institutional reform:

Although he was prepared to fight the Commonwealth for the sake of financial justice, Greiner's overriding concern remained one of rationalising and reforming the relationship. Tactically and strategically it suited his cause to forge a link between Hawke's interest in microeconomic reform and a redistribution of responsibilities and a fairer financial relationship within the Federation (Hancock, 2013, p. 252).

Greiner took advantage of the new reform drive by releasing his *Facing the World* vision. Its goal was to improve the economy and living standards whilst maintaining NSW's AAA credit rating. According to Greiner (1992, p. 4), "all of the major reforms...have contributed to turning NSW into an open, competitive and confident community...and that we cannot isolate ourselves from the rapid changes that have been taking place in Europe and Asia". NSW was also better positioned than the other states to take advantage of developments in IT, finance, education, health, and tourism. However, Australia's small and fragmented domestic market meant that Australian businesses were at a disadvantage because of its inefficiencies. Greiner (1992, p. 9) believed that because "Australia has suffered a more severe economic downturn [that suggested] domestic factors are contributing to Australia's relatively depressed position". If Australia and NSW were to become "a centre for European and North American investment into Asia", these inefficiencies had to be addressed (ibid., p. 14). Hence the importance of the SPC process and Greiner's commitment to it, particularly its microeconomic reforms. Even though Greiner's broad reform agenda did not succeed in all areas, particularly fiscal reform and industrial policy, "microeconomic reform was a clear case of policy shift" (Laffin & Painter, 1995a, p. 270). Labor Premier Bob Carr actively promoted these reforms upon winning the March 1995 election (ibid., p. 280).

Victoria: reluctant reformer

Victoria is the manufacturing heartland of Australia, with Melbourne as Australia's most industrial city followed by Geelong, 75 kilometers to the south west. Its industrial concentration means that unions are predominant. It also contains the continent's most arable land. Although

today Melbourne is a bustling cosmopolitan city, a prime example of urban living,¹⁴⁵ it was not always so. To say that Victoria was an economic basket case in the late-1980s and early-1990s is an understatement to those who lived through it. Overall industrial strife and the high number of strikes were dramatically visible signs of the upheaval being caused by Australia's economic transition.¹⁴⁶ All was not well in the so-called 'Jewel in the Crown'.

Former Labor Premier John Cain disagrees of course. Cain could claim, up to 1988, the highest economic growth rate of any state and relatively low unemployment: 86 consecutive months of "by far the lowest rates of unemployment" (Cain, 1995, pp. 160-161). The figures were a result of Cain's response to the moribund state of the Victorian economy in the early-1980s: increase public sector investment with "massive injections of capital" (Cain, 1984, p. 2). For this Cain had the support of voters, unusual for Labor since Victoria's middle class and urban characteristics make it a 'natural' Liberal Party state. Therefore, "the current Victorian voter preference for the Labor Party [is] not a social choice but a political preference for the party perceived as the best economic manager" (Holmes, Halligan, & Hay, 1986, p. 29). Such support for its policies was not matched at federal level. Cain believed that the "Federal Treasury had always opposed the interventionist and Keynesian approach of the Victorian government...[The Treasury] has always resented States having any view at all about economic, monetary or fiscal issues" (Cain, 1995, p. 159).

¹⁴⁵ See The Economist (2015), "Globe Liveability Ranking".

¹⁴⁶ Melbourne was brought to a standstill throughout January 1990 when striking transit workers parked their trams on all of the city's major routes. Victoria then witnessed its largest public demonstration ever on 4 January 1991 (Bottom, 1991).

Cain's interventionism directly contrasted with the market-liberalism and monetarism of Hawke and Keating. They sought to reduce the role of government, eliminate Australia's fiscal and current account deficits, and open up the capital markets and wider economy to more international trade and competition. With tariff levels falling, and further cuts to come, Victoria's protected manufacturing sector was insecure. According to Cain, "we were seen to be moving against the tide of federal economy...policies. For this reason we were not just brushed aside but were actively opposed" (Cain, 1995, p. 161).

Cain believed the real culprits of Hawke and Keating's liberalization policy were Canberra bureaucrats, who not only "had far more power over the federal Cabinet and its key committees than the Caucus or its policy committees" but also "captured the premiers' conference so completely [such that they] make decisions the national government puts to the States as a *fait accompli*" (Cain, 1995, pp. 160-161). The same economists who supported Cain's activist industrial policy identified that the Industry Commission's view on policy had a major impact on the Commonwealth's position (Mahony, 1993). Indeed, the Industrial Commission examined other development models and concluded that "it is naïve to argue that the success of Japan and [Korea, Taiwan, Hong Kong and Singapore] can be explained principally by governments providing industry-specific assistance...[A]ny specific support was broadly market conforming and was normally withdrawn within a relatively short period of time" (Industry Commission, 1990, p. 1). Rather, Australia should focus on microeconomic reform to remain competitive.

Nevertheless, according to Considine and Costar (1992b, p. 1), after his election in 1982, Cain "put in place one of the most extensive programmes of political and economic change to be found anywhere in post-war Australia". Whilst Bannon could not right the SA economy, it

appeared from the outset that Cain could right Victoria's owing to its size and economic sophistication. Cain's Labor Party had the support of a wide array of interests, from unions, teachers, and environmentalists, all of whom arose during PM Whitlam's era of reform and were then shut out by Fraser's Liberal government (ibid.).

Cain's reform programme sought to expand Victoria's export markets by focusing on its competitive strengths, or in other words, by intervening in the marketplace. The government identified several areas ripe to grow their exports, including aluminium smelting and its downstream industries, car manufacturing, natural gas production, and high-value agricultural production and value-added products (Government of Victoria, 1987). The end goal was not unlike the mantra Hawke adopted in the late-1980s but in 1984, critics – including the Commonwealth – believed “it involved a direct assault on the dominant neo-classical economic paradigm because it gave an important role to government in identifying and enhancing the state's portfolio of competitive strengths” (Davidson, 1992, p. 37). Over in NSW, Greiner was critical of too much government involvement in enterprises (Sturgess, 1992). Even though Victoria's government spending growth was less than that of the other states between 1982 and 1992 (Davidson, 1992), the policy of state intervention was eventually replaced with the policy of improving competitiveness. One reason this occurred was due to the failure of managerial reforms to the public service, which included program budgeting, corporate goal-setting and planning, and a reorganization of senior bureaucrats. According to Considine (1992, p. 196), “Victoria led the way and suffered the consequences of having to experiment with ideas and management structures which were often untested and sometimes inappropriate”. Greiner paid some tribute to this, noting that the

experiment of the Victorian and WA Governments were disasters...As a result...there has been agreement among the Governments of Australia...that we should be getting back to the 'nuts and bolts' of government. Indeed, that is one of the reasons why we have been able to achieve historic microeconomic reform in such a short period of time through the SPC (Sturgess, 1992, p. 254).

By 1987, Victoria was expounding the same concern for Australia's competitiveness as was the Commonwealth. The government admitted that "while the necessity for policy to emphasize competitiveness and to improve the position of the trade exposed sector was not so widely realised in 1984, Australia's recent trading problems and broader world developments have led to these themes being widely accepted as the correct basis for policy" (Government of Victoria, 1987, p. 4). Despite acknowledging the crisis in the economy, Cain continued to believe interventionist policies were the correct way to address the economic reform challenge: "The Victorian Government unashamedly adopts an initiating role in seeking to change the structure of the Victorian economy...rather than relying on market forces alone to generate this change" (ibid., p. 10). Whilst some of these measures were effectively microeconomic reforms, the main thrust of the initiatives were tied to the fiscal trouble Victoria was experiencing.

The results of Cain's reforms were high growth and low unemployment yet his policies also led directly to the 1990-91 recession's much stronger impact in Victoria than elsewhere. From Sturgess's point of view, "as the Victorian Government discovered..., if the Reformer's model is seriously flawed, then society as a whole may wind up paying a heavy price" (Sturgess, 1992, p. 219). The Commonwealth's cuts to tariffs in the textiles sector did contribute to some unemployment but the bulk of job losses originated in the public sector due to the fiscal crisis (Dixon & Mahmood, 2008). Major job losses were in "construction, finance, property and business services; and wholesale and retail trade sectors" (Davidson, 1992, p. 27). Employment

fell by 7.5% in Victoria compared to 2.9% in NSW between June 1989 and June 1992 (Dixon & Mahmood, 2008). Davidson (1992) contends that government spending and higher taxes alone cannot explain the severity of the Victorian recession. Rather, the collapse of the Farrow Group of building societies in 1990, which froze A\$1 billion in deposits, and substantial losses at the Victorian Economic Development Corporation¹⁴⁷ – created to intervene and enhance competitive strengths – exemplified the precarious state of Victoria’s finances and shattered confidence in its government and economy. Victorian finances were essentially a house of cards, with significant investments relying on government finances. With the collapse of public sector financing, conducting business in Victoria became very expensive, subsidies to businesses suddenly dried up, and the public service stopped expanding. The state was forced to sell the State Insurance Office, Gas and Fuel Corporation, State Electricity Commission, several investments in mining and agriculture, state land, jails, schools, hospitals, day cares, fire stations, buses, and trams (Bottom, 1991). Cain’s policy of intervention may have contributed to short-term growth but it was “less competent at targeting new industries and restructuring old ones” (Considine & Costar, 1992a, p. 283), two key elements of longer term growth in an era of tariff-free trade. In the end, “the recession of the 1990s focused on gross political mismanagement” (Bottom, 1991, p. 203).

Since reducing costs is one of the primary goals of microeconomic reform, when Hawke proposed a ‘closer partnership’, Victoria accepted despite the bad blood between the Victorian and Federal branches of the Labor Party. The Victorian economy needed reforming but for some in the Victorian Labor Party it seemed that the Commonwealth’s cuts to state transfers in the late-1980s were designed to force the pace of microeconomic reform at the state level. Walsh

¹⁴⁷ Equaling A\$100 million of taxpayer funds.

(1991, p. 7) argues that at times policy failures at the state level “almost certainly have been induced or exaggerated by the degree of [VFI]”. Cain also believed that Labor MPs from Victoria did not defend the interests of their state in the federal Parliament or within caucus: “we had some Victorian ministers [in the federal cabinet] opposed to us on important issues”. This speaks to Hawke and Keating’s ability to lead the charge of reform despite misgivings within the government caucus. The ability to sell reforms within the party would return as a critical issue when Keating sought to oust Hawke as party leader in 1991. Before that, it seemed that the federal government was predisposed to the influence of NSW (Cain, 1995, p. 173).¹⁴⁸

Victoria also accepted Hawke’s commitment to VFI reform. Vic Labor’s 1992 state re-election strategy included all the central themes of the Hawke government’s reform strategy: debt reduction and increased economic efficiency and investment (Kirner, 1991). Premier Joan Kirner, who replaced Cain after his resignation, stated “I’m not a States righter, never have been. The major issues are a matter of national interest” (Gill, 1990). When Jeff Kennett’s Liberals replaced Labor in government, Victoria was fully committed, along with the Hawke government, to eliminating the current account deficit (Stockdale, 1992). Keynesianism and interventionism were out, neo-liberalism and microeconomic reform were in. Whilst NSW and SA led the states, Victoria was a reluctant follower. An “aura of despair” hung over Victoria in 1990, “as a once-resilient State faced a long haul of revision and recovery” (Bottom, 1991, p. 208). That long haul is now known as the ‘Kennett Revolution’.¹⁴⁹

¹⁴⁸ Keating himself was from the more right-wing NSW branch of the Labor Party, which was instrumental in bringing down Hawke in December 1991. Cain may have been correct since Hawke and Keating at times were far ahead of the federal Labor caucus on reform issues.

¹⁴⁹ See Costar and Economou (1999). Nahan (1994, p. viii) states that by 1994, Victoria had the “most thorough reform programme of any Australian Government”.

Queensland and Western Australia: independent but committed reformers

Queensland and Western Australia are the 3rd and 5th largest economies in Australia, respectively. For most of the past 20 years, they have also been two of the fastest growing. Unlike the other states, QLD and WA are heavily reliant on resource production and export. In QLD, agriculture, mining, and tourism comprise the bulk of the economy whilst in WA mining and energy are king and queen. Thus, both are referred to as Australia's 'resource states'.

Politically, QLD was dominated by Country Party Premier Johanne Bjelke-Petersen, who governed for 19 straight years.¹⁵⁰ His conservative politics, strong arm tactics, and almost single-handed running of the government made him a controversial politician. At the national level, Bjelke-Petersen refused to cooperate and maintained a stance of permanent opposition to Canberra when it was under Labor control and continued to struggle for state's rights under the Liberals. He referred to PM Whitlam as a "'feudal lord,' an analogy which suggests that Bjelke-Petersen occasionally felt like a vassal" (Wear, 2002, p. 180). If Bannon could not get his reform of service duplication and overlap off the ground in 1986, then Bjelke-Petersen's intransigence was one of the reasons why. Another was that his government could live off of QLD's resource revenues in an era of high commodity prices. Bjelke-Petersen appealed consistently to a booming economy and to Queenslanders' fundamental values¹⁵¹ in order to win re-election after re-election. Significant reform was deemed unnecessary yet underneath the surface the economy was desperate for change; it had relied for too long on state government direction (R. Scott et al., 1986). After Bjelke-Petersen resigned on corruption allegations, two successive

¹⁵⁰ See Wear (2002).

¹⁵¹ See R. Scott, Coaldrake, Head, and Reynolds (1986).

Country (renamed National) Party leaders could not prevent the election of Labor Premier Wayne Goss in December 1989.

Goss won on a “clear mandate to reform the system of government in Queensland” (Stevens & Wanna, 1993, p. 2). Everything from the police force to the electoral system to the public service was on the reform agenda. The nature of Goss’s reform agenda paralleled that of both Bannon and Greiner and he became a partner in their effort to reform the Australian economy. Seeking to reassure voters, who were unused to Labor in government, Goss promised no new taxes; reform would be funded from economic growth (*ibid.*, p. 4). Growth continued in the resource sector but overall the economy did not see major industrial development and diversification during Labor’s first term. The party’s policies were conservative and recognized the limits of state governance over the economy (Ryan, 1993), in stark contrast with how Labor governed Victoria for most of Cain’s term in office. But QLD Labor’s continuity with the National Party’s economic policies was not matched at the IGR negotiating table. Goss actively participated in the 1990 Premiers’ Conference dust-up, referring to it as “low grade, political theatre”. He continued: “the pretense that Premiers’ Conferences embodied an equal exchange between the several parties to the federation was belied by the reality” (Goss, 1995, p. 2). Faced with an election due in 1992 (and held in September), a long-list of reforms still to undertake, a tight fiscal situation, and an increasingly restive citizenry (many of Labor’s traditional allies protested the government in the lead up to the election), Queensland was ready to accept Hawke’s call for a ‘closer partnership’.

Western Australia is famous, perhaps infamous, for being the only state to vote on leaving the Commonwealth. A 1933 vote supported secession but because the separatist government was voted out of office in a simultaneous state legislative election, the new pro-Commonwealth Labor Party government was left to carry on with separation. It sent a delegation to London to request the dissolution of the Australian federation, which the British House of Commons refused since the delegation did not have the support of Canberra as required by the Statute of Westminster. The change that did occur from these events was the creation of the Australian Grants Commission, which was designed to oversee equalization transfers, thereby countering the secessionist view that Australian fiscal federalism was unfair to Westerners. WA since then has settled into its roles as 'have-more' state, agitator against Commonwealth 'centralism,' and reluctant participant in IGR.

By the late-1980s, WA was experiencing yet another resource boom. Its Labor government, however, was dogged by scandal regarding government investments that had managed to avoid the transparency and accountability normally required of government corporations. State-led development was a hallmark of the WA economy, a policy which received heavy criticism from Canberra and the other states (Gallop, 1986). Many of the more recent investments were in failed businesses, notably Rothwells Bank, petrochemicals, and construction. Allegations of corruption against Premier Brian Burke, who established the fund, and his successor Peter Dowding, who tried to prop-up the insolvent Rothwells Bank, led both men to resign from office. Carmen Lawrence, an opponent of Burke within the Labor Party, replaced Dowding as Premier in February 1990. By the time of Hawke's 'closer partnership' proposal in July, the government was engulfed by demands for a Royal Commission into

allegations of corruption, which was finally established in November. Focused on saving her Labor government, Lawrence had little political capital to fight Canberra, especially when it was run by WA Labor's sister federal party, which helped to soothe the old antagonism between WA's state-led development based on foreign capital and the presence of tariffs that impact WA's resource sector to the benefit of the older, Eastern states (ibid.).¹⁵² In March 1991, Lawrence's government was reduced to a minority when three Labor MPs sat as independents; Labor was eventually ousted at the 1993 election. In this particular case, electoral interests, party affiliation, and the economy all served to dampen WA's usually tense relationship with the rest of the federation.

With all the states¹⁵³ accepting Hawke's call, the stage was set for a whole new way of conducting Australian IGR. Economic circumstances in each state increasingly demanded microeconomic reforms. All politics is local however, and certain circumstances related to electoral incentives contributed to the need for cooperation, or at least to getting results.

The next section outlines how the SPC process unfolded and why a seemingly momentary and circumstantial spark of intergovernmental cooperation was maintained and eventually institutionalized. It begins a couple months after Hawke and Greiner delivered their speeches at the NPC endorsing a 'new federalism' initiative. Between October 1990 and May 1992, a total of three SPC summits were held – in Brisbane, Sydney, and Canberra – and one Premiers-only summit in Adelaide, which together were a manifestation of the continuous negotiation mechanism. During this time, negotiations on economic reform continued and eventually

¹⁵² Sturgess (1993) recalled that the ability of WA and QLD to overcome their parochialness spoke to a genuine change in attitude.

¹⁵³ Tas, NT, and ACT are not covered here because they are far too small to have stopped the process.

expanded to incorporate IGR institutional reform. Heavy usage is made of archival research to document the negotiations, focusing on the reasons why institutional change was deemed necessary and the reasons why actors committed to it to such an extent that they founded COAG.

The Special Premiers' Conferences

Brisbane: continuous negotiation engaged

October 1990 was the beginning of a new era in Australian intergovernmental affairs: it promised more cooperation, effectiveness, and productivity. Yet the HoG heading to Brisbane could be forgiven for thinking that the more things change, the more they stay the same. Their economic, financial, and political crises opened the door to cooperation. Getting results would be a completely different endeavour. Nevertheless, they had now locked themselves into a process of continuous negotiation.

During preparations for the first SPC, SA officials noted some hesitation on the part of the Commonwealth to draft a joint paper on financial relations.¹⁵⁴ Other issues up for joint papers were mutual recognition and duplication of services. Microeconomic reform of railways, roads, electricity, and water were to be handled separately prior to the first SPC. SA suggested that certain principles should underline every issue. These included revenue raising taking responsibilities into account, states facilitating the Commonwealth's fulfilment of its responsibilities, that states dominate service delivery, avoiding overlap and duplication, reviewing tied grants, maintaining fiscal equalization, and the harmonization of regulations.¹⁵⁵

¹⁵⁴ CJ Sumner Collection, State Records of South Australia (herein CJS), GRS 6530/1, Box 4, Folder: Federal/State Relations 1990, "Memo from the Economic and State Development Committee re: Premiers' Conference on Federalism," 30 August 1990, p.1.

¹⁵⁵ *Ibid.*, p.3.

The states produced a paper on reforming Commonwealth-state fiscal relations. It began by acknowledging the need for reform, which “was particularly evident at the June 1990 Premiers’ Conference” and was also noted by Bob Hawke.¹⁵⁶ Addressing this “key issue” for the upcoming SPC “will also facilitate reform of other areas of Commonwealth-State relations (eg [sic] duplication of functions and services)”.¹⁵⁷ An EPAC report in July confirmed this when it stated “federal financial relations arrangements are the single most significant obstacle to a shake-out of intergovernmental duplication” (Wiltshire, 1990, p. 8). The state fiscal reform paper stated that even though reform would take time, other areas could be fixed immediately, such as increasing the certainty of state budgeting with a longer term funding formula for state transfers. As well, tied grants were wasteful and should be reviewed such that state responsibilities are funded from general transfers and not through specific purpose payments.¹⁵⁸ In a joint paper, the Commonwealth and states acknowledged that “the dominance of the Commonwealth Government in federal finance gives rise to a very large proportion of the concern about overlapping and duplication between levels of government”.¹⁵⁹ If areas could not be completely separated, then a way should be found to meet objectives with a clear statement of roles and responsibilities. When they could be separated, “appropriate transfer of funding would be required”.¹⁶⁰ Therefore, even before the process was underway, both orders of

¹⁵⁶ NLA, Papers Prepared for Special Premiers’ Conference Brisbane 30-31 October 1990: “Agenda Papers, Reform of Commonwealth – State Financial Relations (States Paper),” p.1.

¹⁵⁷ Ibid., p.3.

¹⁵⁸ Ibid., p.4.

¹⁵⁹ NLA, Papers Prepared for Special Premiers’ Conference Brisbane 30-31 October 1990: “Agenda Papers, Duplication of Services (Joint Commonwealth – State Paper),” p.2.

¹⁶⁰ Ibid., p.7.

government were in agreement that the VFI and microeconomic reform would both be included in any package deal.

SA Attorney General Chris J. Sumner considered advising the Department of Premier and Cabinet (DPC) that any reorganization of powers and responsibilities “be conditional upon a new financial arrangement whereby the States can impose and raise most of their revenue”.¹⁶¹ According to Sumner, “both the ideas of deregulation and seeing Australia as a nation, particularly in economic terms, are all part of the agenda of changing attitudes, changing the mentality of Australia towards a more productive, competitive environment”.¹⁶² He continued, “the environment for economic reform which now exists must be translated into the area of government”.¹⁶³ Constitutional reform was not going to achieve IGR reform, therefore “we will also need to look at referral of powers legislation...or we need to look at more effective intergovernmental agreements to deal with this problem”.¹⁶⁴ One area suggested for transfer to the Commonwealth was industrial relations.¹⁶⁵

The transfer of power proposal demonstrated that the states were serious about reform in order to avoid overlap and duplication if the Commonwealth was serious about fiscal reform. Industrial relations was one area where Ministerial Councils were cooperating effectively. The time was right “to open positive discussion which may lead to the ultimate integration of federal

¹⁶¹ CJSC, GRS 6530/1, Box 4, Folder: Federal/State Relations 1990, “To the Attorney-General re: Premier’s Conference of Federation,” 25 July 1990, p.2.

¹⁶² CJSC, GRS 6530/1, Box 4, Folder: Constitutional Restructuring 1990, “Speech by CJ Sumer Attorney-General of South Australia at the Commercial Law Association Lunch,” 17 July 1990, p.2.

¹⁶³ Ibid., p.5.

¹⁶⁴ Ibid., p.8.

¹⁶⁵ CJSC, GRS 6530/1, Box 4, Folder: Federal/State Relations 1990, “To the Premier re: Transfer of State Industrial Relations Powers to the Commonwealth,” [no date], p.1. NSW also proposed handing over industrial relations, see Hancock (2013, p. 253).

and state systems into one central system”,¹⁶⁶ which could be accomplished via the Constitution’s s.51 (xxxvii) allowance for federal legislation in areas of state responsibility if the state(s) agree. Industrial relations was an exception, however. Generally speaking, the issue of ‘state’s rights’ was having a debilitating effect on moving Australia towards internationalization in many other policy areas.¹⁶⁷ Greiner even admonished his own Liberal Party for sticking to the old tenets of state’s rights: “Liberals had to abandon their obsession with ‘extreme versions of States’ rights’, and pay more attention to ‘peoples’ rights’”. Greiner went so far as to actually defend Hawke and Keating in a “typical Greiner plea for common sense and rationality” that Europe would soon be more integrated than the Australian Commonwealth (Hancock, 2013, pp. 260-261). Sumner hoped Hawke would speak on these issues, which he did two days later when he delivered his ‘Closer Partnership’ speech.

In the meantime, the Commonwealth prepared its positions. On IGR, it noted that Premiers’ Conferences were generally only for discussing annual budgetary and fiscal issues. Otherwise, “it has been common practice to convene separate ‘special’ Premiers’ Conferences to consider major issues. There have been 14 such special meetings in the period since 1974”. These covered such issues as drug abuse, gun control, and housing.¹⁶⁸ These previous SPCs were different than the upcoming SPC because the former dealt with very specific policy issues. Hawke’s proposed SPC process was to be as broad as possible, including almost every policy area but particularly those areas identified for substantial microeconomic reform. It was also designed

¹⁶⁶ Ibid., p.3.

¹⁶⁷ CJSC, GRS 6530/1, Box 4, Folder: Federal/State Relations 1990, “newspaper clipping: ‘State won’t wither away,’ *The Australian Financial Review*,” 11 May 1992.

¹⁶⁸ NLA, Papers Prepared for Special Premiers’ Conference Brisbane 30-31 October 1990: “Agenda Papers, Premiers’ Conference Arrangements (Commonwealth Paper),” p.2.

to address problems with the Premiers' Conferences as identified by the states. Their complaints included a lack of consultation, no time to analyze the Commonwealth's fiscal offer, few details, and a lack of "genuine negotiation" with the Commonwealth.¹⁶⁹ In response, the Commonwealth proposed that the Brisbane SPC examine ways at improving existing IGR, including an additional Treasurers' meeting, for a total of two per year. The Commonwealth also promised to release its offer to the states a day or two before the Premiers' Conference rather than the morning of. Little mention was made at this time regarding an additional HoG institution besides the annual Premiers' Conference, yet discussions about reforming institutions were clearly occurring as the microeconomic reform effort continued. Transforming the current round of SPCs into a permanent body that could address all policy issues was only an after-thought in the Commonwealth paper.¹⁷⁰ During the early days of the SPC process, substantial institutional reform was not on offer. Bolder ideas were soon to appear.

Preparations for the first SPC also included a joint Commonwealth-state paper on regulatory reform. It stated that "it is essential" that the issue of regulatory difference and inefficiency be addressed if Australia is to have a more integrated and internationally competitive domestic market¹⁷¹ but that achieving uniformity could be a "protracted" process".¹⁷² Complete harmonization in a federation is difficult to achieve if the sub-units are to retain any independence and policy capacity. Yet an efficient and competitive economic union requires

¹⁶⁹ Ibid., p.4.

¹⁷⁰ "The SPC could agree that the annual Premiers' Conference/Loan Council meeting should normally consider only macroeconomic and budgetary matters with separate Premiers' Conferences such as the current SPC being called annually to discuss other matters" (NLA, Papers Prepared for Special Premiers' Conference Brisbane 30-31 October 1990: "Premiers' Conference Arrangements (Commonwealth Paper)," p.5).

¹⁷¹ NLA, Papers Prepared for Special Premiers' Conference Brisbane 30-31 October 1990: "Agenda Papers, Regulatory Reform (Joint Commonwealth – State Paper)," p.1.

¹⁷² Ibid., p.2.

uniform standards. Since harmonization is likely to produce difficult discussions on fundamental issues of state's rights, a way to avoid the problem is to simply recognize each other's standards and when necessary establish a set of minimum standards. That way a good produced in one state is automatically accepted in the other states even if the specific regulations governing it are different. Mutual recognition would allow states to innovate on policy and regulations without generating substantial inefficiencies in the economy.

The paper also took note of similar developments in the EU, whereby certain health and safety regulations considered essential were harmonized, other policies were given minimum European standards, and other were subject to mutual recognition.¹⁷³ Mutual recognition was "used with great skill by the European Commission to produce innovative solutions" in a system where jurisdictions are "jealously guarded". The key factor of success was mutual trust, which is up to "the central authorities to create the material and institutional conditions under which credibility and mutual respect become the most valuable public goods" (Majone, 1994, p. 83). The joint paper concluded that the SPC should adopt mutual recognition and, where it agreed appropriate, to seek harmonization through the Ministerial Councils. Unlike political reform, substantial and potentially arduous economic reforms were high on the agenda. Yet it was the requirement of trust, which Majone identified, that carved a path towards institutional reform.

All in all, preparations for the SPC were progressing. The Commonwealth secretariat in charge of the preparations was headed by Helen Williams. She was the first women to be employed by Treasury and the first to become a departmental head. She recalled just before the Brisbane summit that "there was a buzz in the air, there was excitement. We really felt there was

¹⁷³ Ibid., p.5.

a different way of working together, a different partnership, a real window of opportunity that we all felt we could grab". But institutionalizing the SPC process – by establishing a secretariat, increasing the density of contact between officials, and coordinating with ministerial councils – was still a political game. Mike Codd, Head of the DPMC, advised Hawke that he needed to get the Premiers to agree to a press release before the state advisors could negotiate and alter it substantially. Treasurer Keating was left out of the loop, whether because he refused to be included or because the others knew of his reservations is uncertain (D'Alpuget, 2010, p. 320).

Preparations by the Victorian government provide further insight into state-level institutionalization. The Victorian DPC circulated to all departments a guide on how to help it prepare for the Brisbane summit. DPC was seeking to discover the areas where "major 'duplication' problems" existed, the current IGR processes to deal with them, trends and progress on these issues since 1982, and to "identify specific examples of probably/possible 'early wins' for SPC process (and possible risk areas!)".¹⁷⁴ Authored by the Victoria DPC Steering Committee were reports on several policies, each designed to establish "a process for considering the assignment of roles and responsibilities".¹⁷⁵ Hawke's 'Closer Partnership' speech on duplication's inefficiencies was quoted to give effect to the overviews. Commonwealth involvement in some areas was not necessary whilst in others shared responsibility would continue.¹⁷⁶

Extensive preparations for the Brisbane SPC – especially the joint and separate reviews, the whole-of-government approach within both orders of government, and the goodwill

¹⁷⁴ Public Records Office Victoria, Victorian Archives (herein PROV), Box 11790/P0001 – 000422, Folder: Special Premiers' Conference October 1990, "Economic and social infrastructure, Commonwealth/State Roles, and 'Duplication'," 26 September 1990.

¹⁷⁵ PROV, Box 11790/P0001 – 000422, Folder: Special Premiers' Conference October 1990, "Duplication of Services – Special Premiers' Conference Brisbane," 30-31 October 1990, p.1.

¹⁷⁶ Ibid., p.3.

between actors – resulted in a successful summit. It began with Hawke, who opened the SPC by thanking the Premiers for responding to his July speech: “The positive response that you have made...is the key element. I believe it is the vital spark in giving life, and in giving direction, to this historic process”.¹⁷⁷ It helped of course that all HoG were on the same page as to why a new practice of federalism was needed: “We are agreed that the purpose of setting such a goal is to improve our national efficiency, to improve our international competitiveness, and to improve the delivery and the quality of the services that [governments] provide to the citizens of Australia”. In the past, change had been exceedingly difficult to achieve. But now, Hawke explained, “the response that I have received from you all so far convinces me that never before has the time been so propitious – as indeed, it has never been so urgent and compelling as it is now – for a new effort, a new approach and a new spirit of co-operation”. In other words, economic pressures forced HoG to meet so they might as well make the best of it.

Greiner of NSW then outlined why this summit was special. It was about a shared purpose, one that was not exclusively about money. There were no elections for about 18 months, which presented an opportunity to get down to practical matters, particularly the fact that all governments were “in a period of both revenue and general economic difficulties”.¹⁷⁸ This helped to “convert” all governments to the cause. Lawrence of WA stated that the SPCs’ “emphasis on equal partnership gives all of us an opportunity to demonstrate what are the fundamental strengths of federalism,...[particularly] a capacity to reach agreement on national priorities and to act in the national interest [and] to ensure that there can be a flexible response and that there

¹⁷⁷ NLA, Special Premiers Conference Brisbane 30 October 1990, “Record of Conversation,” p.1.

¹⁷⁸ Ibid., p.2.

can be variation and innovation too”.¹⁷⁹ Bannon of SA then spoke about the history of the Premiers’ Conference. He reminded his colleagues that the people of Australia regarded federalism as the appropriate way to address the country’s problems, despite tense Commonwealth-state relations: “That means, of course, that we are in a partnership”.¹⁸⁰ Michael Field of Tasmania indicated that this SPC could not have happened without the support of the Australian people: “They want to see the delivery of services in an effective and efficient way”.¹⁸¹ But change was not guaranteed simply because goodwill existed amongst the HoG: “Getting the result is going to take a high level of commitment from the people around this table”. Greiner’s efforts in particular won him plaudits from the other Premiers, all of them Labor. A senior political correspondent called it “Nick Greiner’s conference” (Hancock, 2013, p. 264).

When all was said and done, each and every Premier mentioned the VFI. Bannon was the most direct in stating that the Commonwealth’s practice of unilaterally deciding on transfers to the states was a major issue. It was hoped that the SPC process “can mark a more rational partnership approach to...questions of finance”.¹⁸² With the opening speeches concluded, the public part of the summit was over; time for the real work to begin.

Afterward, Greiner stated that the Brisbane SPC was “the most constructive thing I’ve done in two and three-quarter years as premier”. Victorian Premier Kirner, “who did not much care for Hawke, said...‘thank you for having the vision and the leadership and the patience to enable this conference to happen’” (D’Alpuget, 2010, p. 320). Even though the SPC did not take

¹⁷⁹ Ibid., p.4.

¹⁸⁰ Ibid., p.5.

¹⁸¹ Ibid., p.6.

¹⁸² Ibid., p.5.

specific actions in every policy area, HoG were invited to consider further policy reviews and to “note that progress will be reported at future SPCs”.¹⁸³ Hawke was adamant that the process tackle reforms “across a broad front – indeed, across the broadest possible front: the entire economy”.¹⁸⁴ From the start of the SPC process, continuous negotiation was paramount.

One way in which the mechanism of continuous negotiation added institutional reform to the agenda of economic issues was via the establishment of the Committee on Regulatory Reform.¹⁸⁵ One of the Committee’s tasks was to remove inefficiencies in the national market that arose from the regulatory regimes of different jurisdictions. It was all part of Hawke’s belief that the SPC “introduced a new, commonsense, constructive dimension into Commonwealth-state relations”.¹⁸⁶ Australia faced the prospect of having more internal trade barriers than the EU after the signing of the Maastricht Treaty “despite Australian being free of the deep-seated, historical mistrust that has characterised relationships among some EEC countries, and despite our not being inflicted...with the burden of substantial differences in cultures and legal systems”.¹⁸⁷ Mutual recognition of standards was the preferred choice for all areas where uniformity was not vital to the Australian economy. Areas that were considered vital were transport and

¹⁸³ PROV, Box 11790/P0001 – 000422, Folder: Special Premiers’ Conference October 1990, “Reviews in Community Services and Health – Special Premiers’ Conference Brisbane,” 30-31 October 1990, p.4.

¹⁸⁴ NLA, Speech by Bob Hawke at the Confederation of Australian Industry Annual Dinner, 8 November 1990, p.7 (see also <https://pmtranscripts.dpmc.gov.au/release/transcript-8187>).

¹⁸⁵ FOI Request, Department of Premier and Cabinet, State of Victoria (herein FOI Victoria), 02-070515-1-Part 6, “Report of the Committee on Regulatory Reform to Heads-of-Government, Conference of Premiers and Chief Ministers, Adelaide,” November 1991, p.6.

¹⁸⁶ NLA, Hawke at the Confederation of Australian Industry, 8 November 1990, p.7.

¹⁸⁷ PROV, Box 12549/P0003 – 000288, Folder: Special Premiers Conference Committee on Regulatory Reform, “Report of the Committee on Regulatory Reform to the Commonwealth/State Steering Committee – A Discussion Paper on Mutual Recognition of Standards and Regulations in Australia,” May 1991, p.3.

communications:¹⁸⁸ “This was an important decision and is seen as a vital element of the microeconomic reform agenda”.¹⁸⁹ It also indicates the substantial workload the SPC process was handling and the need for negotiations to continue.

With the SPC process underway, the Commonwealth was confronted with more evidence of the scale of the 1990-1 recession. Financial market liberalization was insufficient to stave off increasing deficits and inflation; in fact, floating the dollar and reforming the banking sector had helped to stoke investment, leading to increased capital flows, which in turn created the imbalances. Keating’s determination to stick to his guns on reversing the current account deficit prompted him to state in November 1990 that the recession was one “that Australia had to have” (quoted in Conley, 2009, p. 109). He was correct in that some adjustment was inevitable given the government’s reform programme (EPAC, 1992) (Keating was later vindicated when, after the adjustments had concluded, Australia saw 20-plus years of economic growth). Whilst a political blunder at the time, in retrospect the honesty of the remark places the Commonwealth’s insistence on austerity back at the June 1990 Premiers’ Conference into sharper focus. It also gives an additional perspective on the SPC process: it was about long term, fundamental reforms to the entire economy as much as it was about spinning a positive narrative on the government’s handling, or perceived mishandling,¹⁹⁰ of the 1990-91 recession. Now that the first SPC was successfully completed, the hard work on righting the situation could begin. The comment also gives perspective to “one of the most significant policy statements of [Labor’s] 13 years in office”

¹⁸⁸ PROV, Box 12549/P0003 – 000288, Folder: Special Premiers Conference Committee on Regulatory Reform, “Report of the Committee on Regulatory Reform to the Commonwealth/State Steering Committee – Report to Commonwealth-State Steering Committee,” May 1991, p.3.

¹⁸⁹ Ibid., p.1.

¹⁹⁰ In fact, from this comment can be traced the beginning of the end of Hawke’s premiership (see the June 1990 budget below).

(Conley, 2009, p. 110). With Australia still in recession, and the second SPC planned for July 1991 in Sydney, the Hawke government was ready to finally implement the Garnaut Report's recommendations.¹⁹¹ In March 1991, it launched its next reform drive, entitled 'Building a Competitive Australia'.

Hawke acknowledged that the recession was "sharper, deeper and more prolonged than we anticipated".¹⁹² The government had to act, and do so immediately. The 'competitive Australia' program was designed to reshape the Australian economy for the longer term (short term "palliatives" were not on offer).

This tough, increasingly competitive world...does not owe, and will not give, 17 million Australians an easy prosperity. The days of our being able to hitch a free ride in a world clamouring, and prepared to pay high prices, for our rural and mineral products, are behind us. From this fact flows everything else.¹⁹³

Australia needed to produce more, export more, and import less. Reshaping the economy was the only way to achieve these objectives. The program was substantial: an end to subsidies that were protecting uncompetitive industries and inflating prices, lowering taxes, employment adjustment and training programs, and initiatives in education and research. These last provisions, which included opening fifteen Cooperative Research Centres, were designed to give effect to Hawke's 'clever country' promises from the 1990 election (Hawke, 1994).

Another aspect of the new program was not only external trade but the domestic market as well. EPAC backed an aggressive approach, reporting that the notion of competitiveness being applied only to the trade-exposed sectors "while leaving untouched vast areas of economic

¹⁹¹ EPAC also issued a strong recommendation for competition reforms at the company level in January 1991, which Hawke hoped will act "as a catalyst for action" (EPAC, 1991b).

¹⁹² NLA, Parliamentary Statement by Bob Hawke, "Building a Competitive Australia," 12 March 1991, p.2 (see also <https://pmtranscripts.dpmc.gov.au/release/transcript-8270>).

¹⁹³ Ibid., p.1.

privilege in the rest of the economy, is flawed, both in logic and in history” (EPAC, 1991a, p. 14). EPAC recommended “vigorous [legislation] aimed at promoting rivalry and removing economic privilege” (ibid., p. i). Improving domestic competitiveness meant microeconomic reform, which was continuing, Hawke stated, and, as a result, a more cooperative IGR was taking shape: “In all this, perhaps no issue has achieved the prominence of the waterfront – essential to our export performance”.¹⁹⁴ In other words, the Commonwealth was working with the states to increase productivity and efficiency and reform their port authorities.¹⁹⁵ Similarly, in road and rail transportation, Australian governments were working on achieving more efficiency, and thus more competitiveness. The gains could be achieved if overlap was removed by confining Canberra to overseeing the national highway system (Industry Commission, 1994, p. 23). As well, Hawke wanted an end to the patchwork of rules covering domestic competition, an “important instance of the way we operate as six economies, rather than one”.¹⁹⁶ This issue was front and centre on the Commonwealth’s agenda for the next SPC. Thus, the latest reform drive was not possible without including the states, and involving them meant tackling the fiscal and federalism issues that had proven intractable in the past. Australia could not continue restructuring without continuous negotiation with the states.

The need for IGR reform was now gaining currency. Greiner stated that Australia “could no longer afford to recklessly squander opportunities for legitimate and necessary growth by becoming bogged down in disputes that delay, or deny, the sensible and productive use of our

¹⁹⁴ Ibid., p.7.

¹⁹⁵ NLA, Speech by Bob Hawke at the National Press Club, 13 March 1991 (see also <http://pmtranscripts.dpmc.gov.au/release/transcript-8271>).

¹⁹⁶ Ibid.

natural resources”.¹⁹⁷ Part of the problem was that the various orders of government had not clearly defined each of their rights and responsibilities.¹⁹⁸ The Environment Intergovernmental Agreement, to be discussed at the next SPC, would help solve the problem in that policy area. Agreeing on how to handle Commonwealth interests versus state responsibilities required “political will”.¹⁹⁹ To get a deal, it was proposed that the states give up powers on the environment in order to retain full powers over health and education.

The Victorian analysis of this proposal stated that pollution knows no boundaries yet “the same could equally be said of other important issues like education, yet we still need to act locally,”²⁰⁰ particularly because environmental and land planning issues have huge regional diversities that Canberra could not possibly handle effectively. This did not mean that a national approach was incorrect, in fact the case for it “is very strong”, but national did not necessarily mean Commonwealth.²⁰¹ It is evident here that the states were seriously considering a revamp of IGR at the same time as they were recognizing that they could govern together in the national interest. Rather than continue to centralize in order to produce national policies – as had been the evolutionary pattern of Australian federalism – institutionalized summits could provide an alternative solution to national problems.

Hawke’s ‘Building a Competitive Australia’ speech was well received by the media and public: “it is difficult to overstate its importance, for it transformed Australia’s

¹⁹⁷ PROV, Box 12549/P0003 – 000289, Folder: Special Premiers Conference Environment, “Address by Nick Greiner – Resolving Environmental Conflict: A Political Imperative for the 1990s,” 19 February 1991, p.2.

¹⁹⁸ Ibid., p.12.

¹⁹⁹ PROV, Box 12549/P0003 – 000289, Folder: Special Premiers Conference Environment, “Briefing Note for John Rimmer – Draft Intergovernmental Agreement on the Environment,” 5 January 1991, p.3.

²⁰⁰ PROV, Box 12549/P0003 – 000289, Folder: Special Premiers Conference Environment, “Premier: Trading Environmental Powers with the Commonwealth,” 10 October 1990, p.1.

²⁰¹ Ibid., p.2.

identity...Garnaut's thesis was that closer economic integration between Australia and the Asian region would pay huge export dividends" (D'Alpuget, 2010, p. 324).²⁰² He took his new proposal directly to the nation's press at the NPC. This was the third time Hawke had spoken there in a year's time and he wanted journalists to see his speeches as a trilogy. The first speech was about his Party's vision for Australia (the March 1990 election speech), the second was the 'Closer Partnership' speech on Commonwealth-state relations, which "speeded our course towards [the party's vision]",²⁰³ and now this speech on competitiveness, "the master key to unlock the gates to the kind of Australia we seek" (the one sought by Horne back in 1964).²⁰⁴ The road would not be an easy one, Hawke stated, but it must be taken. Tariffs were now projected to fall to a general rate of 5% by 1996, and the car and textile industries were targeted for cuts, from 35% to 15% by 2000 for cars and to 25% by 2000 for textiles: "The Government has been fortified in this approach by a number of recent reports, not least Dr. Ross Garnaut's report" (Snape et al., 1998, p. 94). It was the government's "proper role...to provide leadership".²⁰⁵

Sydney: institutional reform on the agenda

In the lead up to the Sydney SPC, negotiations on a package deal – and deciding on tradeoffs – were in full swing. The SA director of IGR reported that mutual recognition and competition policy were ready for the SPC. Victoria considered that mutual recognition was alright yet it was ready to go further and agree on national uniformity if others were ready:

²⁰² Hawke (2010, p. 14:20) recounts that "Professor Garnaut has referred to the March 1991 reforms as some of the greatest reforms ever".

²⁰³ NLA, Hawke at NPC, 13 March 1991, p.2.

²⁰⁴ Ibid. Hawke later stated that there were those who said "I'd run out of puff for a fourth term. [Building a Competitive Australia] proves that is crap" (D'Alpuget, 2010, p. 325).

²⁰⁵ NLA, Hawke at NPC, 13 March 1991, p.5.

“There is not a lot direct benefit for [Victoria on mutual recognition] and hence this item is a potential trade”.²⁰⁶ Provisions on uniformity as requested by Victoria were deleted in the draft report to be submitted to the SPC.²⁰⁷ Despite the boldness of the reform program, clearly some were not ready for too much boldness. Likewise, on electricity, there was some pushback from QLD. The SA report noted that “this may be an area in which we could give Queensland some support in exchange for their support in other areas, e.g. Road Transport”.²⁰⁸ Victoria noted that it was ready to ratify the national electricity grid management council²⁰⁹ but that it was still at a disadvantage on road funding since it received only 21% of Commonwealth funding yet accounted for 27% of total kilometers travelled.²¹⁰

On the environment, SA noted that NSW had “gone soft to trade other gains from Commonwealth”.²¹¹ The Commonwealth was unable to decide its position on a federal right to review land use planning and abide by decisions made at the state level.²¹² Taxation reforms and the review of tied grants were seeing “aggravatingly slow” progress. The Commonwealth was slow to commit to untying funding and removing overlap and duplication. However, “scope exists for trade-offs...between the SPC and the Financial Premiers’ Conference”.²¹³ Victoria believed that pushing too much for the untying of grants would be a tactical error on the part of the states

²⁰⁶ PROV, Box 12549/P0003 – 000288, Folder: Special Premiers Conference Working Group on Tied Grants 1, “Premier: Strategy for Special Premiers’ Conference,” 8 July 1991, p.2.

²⁰⁷ PROV, Box 12549/P0003-000288, Folder: Special Premiers Conference Committee on Regulatory Reform, “Letter from Gary Sturgess to Mike Codd re: Report of Committee on Regulatory Reform to Commonwealth-State Steering Committee,” 6 May 1991, p.1.

²⁰⁸ JBC, Folder: Premiers Conference 1991, “Premiers’ Conferences (Financial and Special),” 6 May 1991, p.1.

²⁰⁹ PROV, Box 12549/P0003 – 000288, Folder: Special Premiers Conference Working Group on Tied Grants 1, “Premier: Strategy for Special Premiers’ Conference,” 8 July 1991, p.2.

²¹⁰ Ibid., p.12.

²¹¹ JBC, Folder: Premiers Conference 1991, “Premiers’ Conferences (Financial and Special),” 6 May 1991, p.2.

²¹² PROV, Box 12549/P0003 – 000288, Folder: Special Premiers Conference Working Group on Tied Grants 1, “Premier: Strategy for Special Premiers’ Conference,” 8 July 1991, p.3.

²¹³ JBC, Folder: Premiers Conference 1991, “Premiers’ Conferences (Financial and Special),” 6 May 1991, p.3.

because “there is not a great margin of flexibility in State expenditure even if grants were completely untied. It is recommended that Victoria continues to advocate reform of tied grants but puts its negotiating chips on other issues”. Finding a solution to the fiscal arrangements was fundamental because, in reviewing functional allocations, the general solution was “greater devolution to State and local administration which a framework of national policy and standards, however such an outcome increases the future expenditure demands on the State”.²¹⁴ To get agreement, it was recommended to the Premier that “informal soundings with other Premiers would be desirable” to change the pace and priorities of the SPC.²¹⁵

Despite the slowdown in progress, the Sydney SPC was held at the end of July 1991. Hawke began the summit by outlining the country’s unemployment problem. The Premiers were concerned that austerity would worsen the situation.²¹⁶ The Commonwealth recognized this and agreed “to maintain the level of general revenue assistance in real terms for the next three years”.²¹⁷ The promise was actually first made at the 1990 Premiers’ Conference, when it was needed to get the states back to the negotiating table. This time around the Commonwealth was advocating for restraint but on terms the states could agree with. It also wanted to push for further microeconomic reforms, since it will “produce significant budgetary benefits for the States over time”.²¹⁸ Bannon’s proposal for infrastructure spending was meant to tackle the unemployment problem whilst internationalizing the Australian economy.²¹⁹ As well, HoG agreed

²¹⁴ PROV, Box 12549/P0003 – 000288, Folder: Special Premiers Conference Working Group on Tied Grants 1, “Premier: Strategy for Special Premiers’ Conference,” 8 July 1991, p.1.

²¹⁵ Ibid., p.3.

²¹⁶ JBC, Folder: Premiers Conference, “Premiers’ Conference Transcript,” 31 May 1991, p.1-2.

²¹⁷ JBC, Folder: Premiers Conference 1991, “Premiers’ Conference and Loan Council Meeting: Commonwealth Offer to the States and Territories,” 31 May 1991, p.1.

²¹⁸ Ibid., p.2.

²¹⁹ See JBC, Folder: Premiers Conference, “Letter from Bannon to Hawke,” 23 May 1991 for details of the proposal.

to continue examining the untying of grants and stated that “Commonwealth involvement in operational management should be reduced to the greatest degree possible consistent with ensuring that agreed national objectives are met”.²²⁰

The slowdown in progress, evident even before the Sydney SPC, was at risk of increasing because the work plan after the summit was far more complex than before. In order to manage the workflow, attention began to shift to the structure of the IGR system itself. The Sydney summit sought to tackle the issue by altering Ministerial Councils, which had been the purview of each respective ministry. After Sydney, they reported directly to HoG when they convened as the SPC. Placing the SPCs above the Councils required changes to the way state governments were organized. Vic DPC asked each department to keep it informed of Ministerial Council meeting agendas and minutes “to ensure that Victoria’s views on issues of vital importance are properly developed and presented,” ensuring Victoria’s contribution to the SPCs would be as effective as possible.²²¹ The fact that the DPC was not directly involved in Ministerial Councils prior to this date demonstrates that Premiers’ Conferences were detached from IGR policy-making. It took the SPC process to insert HoG directly into IGR decision-making, a small but significant step toward institutionalizing HoG summits.

The Victorian government was clearly aware of the importance of the SPCs in its working paper on IGR reform: “The interdependence of national economic, environmental and social issues together with the increasing internationalisation of Australian society will require a closer

²²⁰ PROV, Box 12549/P0003 – 000288, Folder: Special Premiers Conference Working Group on Tied Grants 2, “Working Group on Tied Grants: Draft Report prepared for Commonwealth-State Steering Committee Meeting,” 9-10 October 1991, p.2.

²²¹ PROV, Box 11790/P0001-000422, Folder: Special Premiers’ Conference October 1990, “Letter from Peter Kirby, Secretary Victoria DPC to Mr S. Antonelli, Acting Director of Ethnic Affairs,” 28 August 1991.

partnership”.²²² Trust, fairness, flexibility, overall consensus but not necessarily unanimity, and clarity of purpose were necessary for success. Legalism and constitutional reform would not provide these, only new agreements, new institutions, and new norms would “set IGR on a sound footing”.²²³ The Brisbane SPC agreed that a more formal HoG meeting was required in order to expand intergovernmental agreements across a broader range of policy areas, which could then be translated into legislation: “All areas of government should eventually be reviewed by the SPC process”.²²⁴ The Sydney SPC then established a steering committee to engage in national performance monitoring of reforms to Commonwealth and state enterprises in energy, water, public transport, railways and ports (Industry Commission, 1992).

Continuous negotiation on economic policies was clearly having an effect on IGR. HoG were seeing results but understood that maintaining progress required institutional reform as well as fiscal: the Victorian government expected certain results, including “a fair share of the national tax pool, and a more predictable revenue base”.²²⁵ Microeconomic reform was also essential, especially to public services, energy, ports, and transportation: “The proposed National Rail Freight Authority is...a crucial test of the new cooperative federalism, to see that the financial and operation arrangements are genuinely fair and rational, and not just a reflection of the economic muscle of the participants”.²²⁶ Reform to the functional allocation of services was also crucial, as “Victoria believes that there is scope for significant devolution and that the States

²²² PROV, Box 11790/P0001-000422, Folder: Special Premiers’ Conference October 1990, “Letter from Kirby to G. Papadopoulos, Director of Ethnic Affairs,” 5 June 1991, p.1.

²²³ PROV, Box 11790/P0001-000422, Folder: Special Premiers’ Conference October 1990, “Victorian Policy Goals for Intergovernmental Relations Reform,” May 1991, p.2.

²²⁴ Ibid., p.9.

²²⁵ Ibid., p.4.

²²⁶ Ibid., p.6.

should become the primary agencies for policy implementation". The era of parallel Commonwealth, state, and local agencies was over.²²⁷

However, the media was having none of it: "The Commonwealth-state reforms resisted snappy explanation...By this stage the press gallery was so sullen about Hawke that a majority was unwilling to report anything positive about him" (D'Alpuget, 2010, p. 340). The leadership battle between Hawke and Keating was beginning to take its toll.

Leadership is a common thread throughout this narrative, particularly since it concerns primarily the views and actions of heads-of-government. Political leadership enabled the SPC process to begin and achieve results. A leadership contest would then cause the process to falter. Even as Hawke engaged the states in a program of microeconomic reform, he was becoming embroiled in a battle over the leadership of the Labor Party with his Treasurer, Paul Keating.

Keating and Hawke supposedly agreed back in 1988 at Kirribilli House²²⁸ that Keating would succeed Hawke as Labor Party leader soon after the March 1990 election. The agreement was made after comments from Hawke that pointed to his thinking that the Treasurer is dispensable. Keating's reaction at the time was furious: "what he was saying to me was 'the partnership's over' ...This government's got two leaders within it and I'm the other one and you don't treat me like that" (Chubb, 1993, p. Ep.3 39:28). Then in December 1990, Keating made what is referred to as his 'Plácido Domingo' speech.²²⁹ It was supposed to be an off-the-record conversation at the NPC. Yet Keating's comments about Australia requiring strong leadership and

²²⁷ Ibid., p.7.

²²⁸ See Hawke (1994). Kirribilli is the PM's residence in Sydney.

²²⁹ The reference is to the topic of the speech: "the art of leadership as being both about performance, and about music – singing a song" (Simoins, 2003). Plácido Domingo is a Spanish tenor, conductor, and member of 'The Three Tenors'. Keating is well known for his love of classical music and for collecting antique French clocks.

a new vision were widely interpreted as referring to Hawke (despite Hawke's name never being mentioned).²³⁰ This "created a rift of unprecedented dimensions" (Carew, 1992, p. 284), effectively terminating the Kirribilli Agreement and perpetuating a year-long leadership battle.

In May 1991, Keating leaked the details of the agreement, precipitating a caucus crisis. A secret ballot was held for the party leadership, in which Hawke gained 66 caucus votes to 44. Keating then resigned from Cabinet but there was almost no doubt he would try again to oust Hawke: "During the last five months of 1991 the authority of the Hawke government rotted away" (Blewett, 1999, p. 11).²³¹ Part of the reason was the growing popularity of Opposition leader John Hewson, who's 'Fightback!' economic plan for tax and spending cuts was setting the national agenda. The situation worsened when the 1990 budget – the first without Keating as Treasurer since 1982 – was described as "pathetic...meaningless" for not attacking the recession (Chubb, 1993, p. Ep.5 24:05). Hawke's authority was also in doubt because Keating, now a backbencher – but which was "no descent into obscurity" (Carew, 1992, p. 295) – used the SPC process to convince his fellow caucus members that Hawke was weakening the Commonwealth and therefore needed to be replaced.

At the NPC on 22 October 1991, Keating staked out a policy position that was drastically different from his boss': "I believe that one of the gravest dangers we face as a nation today is the dismembering of the national government which would inevitably follow from surrendering revenue and other national responsibilities to the States". This took a dramatically different tone

²³⁰ See J. Edwards (1996). Hawke said "I don't pretend that this sort of reference was not hurtful and disappointing" (Hawke, 1994, p. 498).

²³¹ The media may have played a role in this, especially since Rupert Murdoch controlled the newspaper market and backed Keating; see D'Alpuget (2010). Note too that D'Alpuget is Hawke's wife.

than Hawke's 'Closer Partnership' speech. Keating continued, "I believe that...through putting the desire for agreement ahead of the need for hard analysis, we do risk doing a harm to our Commonwealth".²³² Furthermore, Keating took aim at Hawke's commitment to examine the revenue side of Commonwealth-state relations: "[The VFI] is not a design fault, and does not require remedying".²³³ Australia is too small, he believed, for the Commonwealth to lose control of fiscal policy (J. Edwards, 1996).

Keating went further, attacking Hawke in all but name: "When we wished to change the tax system in 1985 we had a White Paper and months of national debate. But in the run up to what is billed as, and may well be, the most important Federal-State Conference since federation we have had nothing but a few press reports on rumoured changes".²³⁴ Worse still, Premier Greiner and his "allies" were seeking "the dismembering of the national government".²³⁵ Greiner's most important ally in the SPC process was Bob Hawke. After Hawke's ouster by Keating, it was reported that his close confidant and Head of the DPMC, Mike Codd, "must wear some personal responsibility for the failure of Mr Hawke's dream of a new federalism...[because] the structures and procedures he helped establish were criticised, including by Paul Keating, for secrecy and a lack of public consultation, and helped sink it".²³⁶ In his speech, Keating essentially "threw down the gauntlet to both Hawke and the states" (J. Edwards, 1996, p. 448). Later, Keating recalled the federalism speech: "We had to knock [Hawke] senseless without leaving any bruises" (ibid., p. 465). Keating gambled that the Labor caucus if "forced to choose would back [his]

²³² NLA, Speech by Paul Keating at the National Press Club, 22 October 1991, nla.obj-222603988, p.1.

²³³ Ibid., p.2.

²³⁴ Ibid., p.6.

²³⁵ Ibid., p.5.

²³⁶ NLA, Newspapers: Biographical cuttings on Mike Codd, "Mike Codd's departure marks the end of an era," *The Canberra Times*, 28 December 1991.

centralism against Hawke's devolution option" (D'Alpuget, 2010, p. 343). Hawke himself had come a long way from his 1979 lecture on dissolving the states entirely yet he was unable to fully change the Labor Party's views on federalism. Hawke counters that Keating was fully involved in preparing the SPCs and that both men had agreed on the Commonwealth retaining macro-economic policy control (Hawke, 1994). Hawke recounts Keating's arguments as "pretty rough sort of stuff. It wasn't accurate" (Hawke, 2010, p. 14:45). Politics sometimes comes before policy.

Adelaide Premiers' Summit

Hawke wanted the SPC process to succeed but he was being outflanked by his former Treasurer. Premiers Bannon and Greiner had put forth several proposals for the Perth SPC, due for some time in November 1991. This was the culmination of the last two SPCs and represented a real chance to achieve far-reaching reforms. Their package sought a shared national tax to address the VFI and the establishment of a permanent forum for HoG decision-making: "The Premiers said that the reform package would realise the vision for the future of the Australian Federation set out by the PM at the first SPC in October last year".²³⁷ The shared tax would address not only the raising of revenue – by giving the states access to a broad tax base that would reduce their reliance on federal transfers – but also the states' accountability for spending. Changes to the state portion of the tax would be a matter for agreement at a permanent HoG meeting: "The SPC process has demonstrated that HoG can progress beyond the narrow preoccupation of local concerns and achieve long term reforms in the national interest".²³⁸

²³⁷ JBC, Folder: Premiers Conference, "News Release: State proposals for SPC," 8 November 1991, p.1.

²³⁸ Ibid., p.2.

However, the new HoG meeting was not operating just yet. Keating's comments and threat to Hawke's leadership meant that Hawke had to tread carefully. He had already rejected the Greiner-Bannon proposal during Question Time on 11 October 1991 yet stated at the same time that it was simply a proposal and bargaining would continue in preparation for the next SPC. It was still possible to find an agreement because "the government is conscious of the states' understandable concern to achieve a greater degree of certainty in the financial resources available to them".²³⁹ Hawke recalled that the proposal was in committee and that he was "sticking to the bargain...with the States" (Hawke, 1994, p. 535). After Keating's speech to the NPC on 22 October, Hawke promised his caucus there would be no state income taxes (Mills, 1993). On 6 November, the ABC radio news programme 'AM' reported that Keating's "consistent attack" on Hawke's new federalism was risking the SPC process. Premier Lawrence noted that Hawke was moving toward reforming financial relations and recently "backed down on that, whether it's pressure from Mr Keating or the rest of Caucus, I don't know". When asked if the Labor Party leadership struggle was to blame, she stated "well, it appears to be".²⁴⁰ Lawrence noted that the Premiers took Hawke's position on fiscal relations "in good faith [and] we've already made significant amendments to our own positions".²⁴¹ Greiner shot back at Keating, stating that he was "totally selfish and totally hypocritical" (Hancock, 2013, p. 303).

Hawke's balancing and Lawrence's warnings were to no avail. When the federal Cabinet rejected the states' proposal just prior to the Perth summit, Lawrence released a statement cancelling it because "the PM has gone back on his undertaking last year to 'redress the

²³⁹ JBC, Folder: Premiers Conference, "Question Time House of Representatives," 11 October 1991.

²⁴⁰ JBC, Folder: Premiers Conference, "Media Monitoring: Commonwealth-State Finances," 6 Nov 1991, p.1-2.

²⁴¹ Ibid., p.2.

imbalance in Federal/State financial relations’’.²⁴² Hawke had stated he was open to negotiation but “the atmosphere of bitterness and uncertainty about the Commonwealth’s position” eventually proved devastating (Hawke, 1994, p. 536): “The PM has dismissed the major reform on which other reforms were to have been based”.²⁴³ The Premiers were not impressed with “recent squabbling among Federal politicians”. No matter, the Premiers were not about to see their efforts come to naught: “To ensure momentum for essential reform was not lost the Premiers would hold a conference in Adelaide next week chaired by SA’s John Bannon to form the Council of the Australian Federation”.²⁴⁴ Hawke’s plans were apparently in ruins, and it would not be until 2000 that VFI reform would find expression.²⁴⁵

The Adelaide communiqué was clear: reforming the economic union and IGR system required addressing the fiscal imbalance followed by functional reallocation and reducing tied grants. The Premiers were convinced this would lead to better cooperation amongst them and so “agreed that it was possible to advance the important process of reform that had been commenced by the SPC process. For this reason, they agreed to meeting to progress a wide range of matters”.²⁴⁶ After the summit, the Premiers wrote to Hawke. Whilst the summit was a success, they stated that “these fundamental issues can only be addressed by a co-operative and open process involving the Commonwealth”.²⁴⁷ Turns out the states needed the Commonwealth just as much as it needed the states. Holding their state-only summit was meant to continue the SPC process; Bannon’s last-minute hosting of the summit saved the entire process.

²⁴² JBC, Folder: Premiers Conference, “Media Statement: DPC Western Australia,” [no date], p.1.

²⁴³ Ibid.

²⁴⁴ Ibid., p.2.

²⁴⁵ Greiner stated later that “we lost 18 years,” see D’Alpuget (2010).

²⁴⁶ FOI Victoria 02-070515-1-Part 4, “Premiers and Chief Ministers Meeting Adelaide,” 21-22 November 1991, p.1.

²⁴⁷ JBC, Folder: Meeting of Premiers and Chief Ministers, “Letter from Bannon to Hawke,” 22 November 1991, p.1.

Afterwards, the state governments made preparations to continue with the negotiations. Bannon reiterated to his government after the Adelaide summit that a 'whole of government' approach was necessary to consolidate the reform effort.²⁴⁸ As this was "a very sensitive period in Commonwealth/State relations", it was important that all Victorian departments keep the DPC informed of all IGR issues.²⁴⁹ The VFI was still front and centre: "A substantial reduction in VFI is imperative for a more effective federation and a more efficient Australian economy". But it is clear the states did not want this one issue to prevent cooperation in the other areas: "It is essential to reopen the dialogue between ourselves; and the Adelaide summit gave consideration as to how this might be achieved".²⁵⁰

The Premiers' desire to proceed with the reform process was evident when they forwarded to Hawke the final changes to the Intergovernmental Agreement on the Environment and informed him that it "should now be signed".²⁵¹ They also reached agreement on transportation,²⁵² endorsed a national competition policy,²⁵³ and "for the first time, Australia will have uniform rules of the road".²⁵⁴ A feasibility study on interconnecting the power grids of the Eastern states was launched and, to top it all off, the states entered into an agreement on mutual recognition.²⁵⁵

²⁴⁸ JBC, Folder: Meeting of Premiers and Chief Ministers, [no date].

²⁴⁹ PROV, Box 06008/P0001 – 001341, Folder: IGR Reform – Victorian Policy Goals, "Letter from Kirby to J. Langford, Rural Water Commission," 14 January 1992.

²⁵⁰ JBC, Folder: Meeting of Premiers and Chief Ministers, "Letter from Bannon to Hawke (financial arrangements)," 22 November 1991, p.2.

²⁵¹ JBC, Folder: Meeting of Premiers and Chief Ministers, "Letter from Bannon to Hawke (Environment)," 22 November 1991, p.1; see FOI Victoria 02-070515-1-Part 5, p.49 for the Environment agreement.

²⁵² JBC, Folder: Meeting of Premiers and Chief Ministers, "Letter from Bannon to Hawke (Road)," 22 Nov 1991.

²⁵³ JBC, Folder: Meeting of Premiers and Chief Ministers, "Letter from Bannon to Hawke (Competition Policy)," 22 November 1991.

²⁵⁴ FOI Victoria 02-070515-1 – Part 4, "Premiers and Chief Ministers Meeting Adelaide," 21-22 November 1991, p.4.

²⁵⁵ JBC, Folder: Meeting of Premiers and Chief Ministers, "Letter from Bannon to Hawke (Mutual Recognition);" see FOI Victoria 02-070515-1-Part 4, p.30 for Mutual Recognition Agreement.

The communiqué announcing the deal asked the Commonwealth to pass a single Act implementing mutual recognition, “and the States and Territories will effectively cede power to one another through the mechanism of Commonwealth legislation”.²⁵⁶ Federal legislation was preferable to a state-by-state approach in order to lessen confusion and maximize certainty.²⁵⁷ Note that legality is the strongest indicator of routinization (see Table 2). The Committee on Regulatory Reform expressed its opinion that a rush to the lowest common standard would not occur because of standards reviews by Ministerial Councils and because of competition. Mutual recognition would help resolve issues of standards harmonization since these measures were designed to “improve efficiency, promote productivity and generate economic and employment growth”.²⁵⁸ But the commitment of HoG was essential if mutual recognition was to succeed.²⁵⁹ This may include HoG “becom[ing] involved in enforcing agreed standards where no resolution of disputes is achieved through the relevant Ministerial Councils”.²⁶⁰ In other words, mutual recognition represented a significant change to the Australian economic union that technocrats could not achieve without the political authority and impetus of HoG. Such decision-making would not have found expression without HoG summit institutionalization and continuous negotiations.

²⁵⁶ FOI Victoria 02-070515-1 – Part 4, “Premiers and Chief Ministers Meeting Adelaide,” 21-22 November 1991 communiqué, p.2.

²⁵⁷ PROV, Box 12549/P0003-000288, Folder: Special Premiers Conference Committee on Regulatory Reform 3, “Letter from Sturgess to Codd,” 6 May 1991, p.1.

²⁵⁸ FOI Victoria 02-070515-1 -Part 4, “Premiers and Chief Ministers Meeting Adelaide,” 21-22 November 1991 communiqué, p.11.

²⁵⁹ PROV, Box 12549/P0003-000288, Folder: Special Premiers Conference Committee on Regulatory Reform 3, “Report of the Committee on Regulatory Reform to the Commonwealth/State Steering Committee,” May 1991, p.22.

²⁶⁰ FOI Victoria 02-070515-1-Part 6, “Report to Heads of Government,” [no date], p.8.

The Adelaide summit also released four principles that would form the basis of negotiations on each order of government's functional responsibilities (these were originally part of the Premiers' proposal for the now-defunct Perth summit). Principle 1 was deemed the Australian national principle as it recognized that national problems were most likely best solved at the national level. An open and efficient economic union and equity among citizens were expressions of the national principle but that "in the articulation of the national interest the Commonwealth has a primary but not exclusive role".²⁶¹ Principle 2, the subsidiarity principle, was designed to ensure accountability and diversity. Citizens are better served when their preferences are delivered as efficiently as possible by the most accessible and appropriate decision-maker, such that regional diversity can be taken into account.²⁶²

Principle 3 was the structural efficiency principle. As noted above, duplication and overlap were drags on the economy: "Inefficient Commonwealth-State divisions of functions can no longer be tolerated...[but cooperative] arrangements can only be built on legitimately shared objectives, a relationship of mutual trust and economic incentives to cooperate rather than confront".²⁶³ The fourth principle was accountability. IGR should be transparent, which involves comparability and consistency in government programs and fiscal reform. These four principles formed the basis of a framework for future HoG meetings. The Premiers' last-minute organization of the Adelaide summit indicates the seriousness with which the Premiers considered the economic, fiscal and institutional reform process; it represents a significant step towards COAG's

²⁶¹ JBC, Folder: Meeting of Premiers and Chief Ministers, "Letter from Bannon to Hawke (financial arrangements) Attachment," 22 November 1991, p.ii.

²⁶² Ibid., p.iii.

²⁶³ Ibid., p.iv.

institutionalization. As is shown below, the Premiers' proposal was far too developed and too politically important for future PM Keating to ignore.

With principles in hand, the Premiers then sought ways to prevent the rancor that occurred in the lead up to the cancelled Perth SPC. Because the VFI issue was connected to so many other issues, particularly the allocation of functional responsibilities and its four principles, a permanent forum was needed to address them all and to implement the principles. Premiers proposed the Council of the Australian Federation: a formal and permanent mechanism of cooperative federalism²⁶⁴ "with the capacity to consider all of these issues, is the appropriate forum to advance reform".²⁶⁵

The Council proposal is the best evidence of governments' commitment to cooperative federalism. The Brisbane SPC sought to "strengthen the Australian federal structure". In doing so, HoG realized that reforming the economic union required something more: "In every instance in the SPC process where HoG have sought to reach higher levels of cooperation and more mature federal partnership, the need for an on-going, national, high-level decision making forum through which national issues may be addressed has become apparent".²⁶⁶ The SPC process demonstrated the states' ability to act in the national interest both independently and in cooperation with the Commonwealth. The success of the process thus far was due to the recognition that states are not diametrically opposed to national issues. Whether it was reforming the electricity or road networks or reviewing the boundaries between governments'

²⁶⁴ JBC, Folder: Meeting of Premiers and Chief Ministers, "Letter from Bannon to Hawke (financial arrangements)," 22 November 1991, p.3.

²⁶⁵ JBC, Folder: Meeting of Premiers and Chief Ministers, "Letter from Bannon to Hawke (functional responsibilities)," 22 November 1991, p.1.

²⁶⁶ JBC, Folder: Premiers' Conference, "Draft Proposals: A Council of the Australian Federation," Nov 1991, p.1.

functional responsibilities, achieving reform required an institutionalized HoG meeting. A permanent body to debate and define the national interest and implement policy would ensure Australian IGR remain cooperative and effective rather than adversarial.²⁶⁷

The catalyst for IGR reform was mutual negotiation, which required Ministerial Councils to take more decisions, requiring enhancements to their accountability: “Few Ministers take every pending Ministerial Council decision to their own cabinets. This means that in some cases Ministerial Councils act with indirect political accountability”.²⁶⁸ More cooperation between governments needed to be matched by more coordination within them and with the HoG ultimately responsible for intergovernmental decisions. More HoG involvement required a “HoG decision-making body which focuses on strategic cross jurisdictional and cross-portfolio structural issues”.²⁶⁹ The proposed Council would aim for information-sharing and consensus-building and would monitor implementation should decisions be taken. Certain standing issues would be part of its agenda – such as the economic union, coordination of spending and regulatory policies, reviews of functional allocation and international treaties, and the management of Ministerial Councils.²⁷⁰ Economic reform, which launched the entire SPC process, had finally forced political reform.

The First Keating Labor Government

The fact that the Premiers were disappointed with Hawke was next to nothing compared to how former Treasurer Keating felt. By December 1991, Keating was ready to stage a second

²⁶⁷ Ibid., p.3.

²⁶⁸ Ibid., p.2.

²⁶⁹ Ibid., p.3.

²⁷⁰ Ibid., p.4.

attempt to oust Hawke as Labor Party leader. The government was increasingly inept at handling the opposition's economic rebuttals. Cabinet shuffles and growing dissent in caucus all contributed to Hawke's lowest ever approval rating: 26% on 17 December (Blewett, 1999).²⁷¹ By now, the PM's allies were advising him to resign.²⁷² He refused, forcing Keating to call a leadership vote. Hawke lost, installing Keating as leader, and Prime Minister.

Keating was fully aware that what helped him to the leadership was the perceived failure of the Hawke government to deal with both the recession and the opposition's 'Fightback!' plan. "Keating had not defeated Hawke over policy differences" merely his potential ability to win the next election (J. Edwards, 1996, p. 452). Upon taking the helm, Keating began to focus on Labor's own economic plan, called *One Nation*. It was developed on the back of several cabinet discussions. At one of them in early January 1992, Keating was informed that "our micro-economic reforms themselves lead to unemployment" (Blewett, 1999, p. 23). Sturgess's warning from April 1991 was coming true: "if...the PM or the Premiers are diverted by their own immediate political needs, then the momentum of these reforms could well be lost. If that happens, I would suggest that it will be very difficult to re-fire the boilers and get this ship moving once again" (Sturgess, 1992, p. 221).

Perhaps sensing the mood of the Keating government, Bannon wrote to the new PM about the recession, telling him that SA wanted "the acceleration of micro-economic reform through public investment in infrastructure".²⁷³ These reforms were designed to address the fact

²⁷¹ Hawke was the first party leader to attain over 70% approval, back in 1983; see Mills (1993).

²⁷² See also Carew (1992); D'Alpuget (2010); Mills (1993).

²⁷³ JBC, Folder: to the PM Keating Jan 1992, "Submission from the South Australian Government for the Federal Economic Statement," January 1992, p.2.

that SA unemployment was the highest in Australia because of its reliance on manufacturing, which was made all the more vulnerable because of accelerated tariff cuts. Government assistance was required but the real solution was more reform: “Already, significant achievement have been made in the areas of road and rail transport, electricity generation,...regulation of the non-banking financial institutions sector”. To see through the reforms, Bannon urged Keating’s government “to re-commit itself to the principles and the process of consultative reform set in train at the first SPC in October 1990 and to work together with the States and Territories to bring these micro-economic reform initiatives to a constructive conclusion”.²⁷⁴ Signing the mutual recognition agreement was also critical.

One Nation was released on 26 February.²⁷⁵ It was premised on Australia entering a low inflation, high productivity recovery. Government would assist with stimulus spending, including major investments in infrastructure, reversing years of austerity. What Hawke could not do in 1990, Keating could do in 1992. *One Nation* also sought to strengthen export competitiveness, cut taxes, and reshape the Prices and Income Accord towards direct bargaining between labour and business.²⁷⁶ It also included microeconomic reforms to railways, electricity, and aviation (Watson, 2003). Worries remained²⁷⁷ but the recession and the opposition had to be dealt with if Labor was to win re-election in 1993.²⁷⁸

²⁷⁴ Ibid., 8.

²⁷⁵ See Watson (2003), Keating’s speech writer at the time.

²⁷⁶ See J. Edwards (1996).

²⁷⁷ EPAC noted in 1994 that “the international business cycle have overwhelmed the early pay-off from microeconomic reform. However, Australia is now very well-placed to take major advantage of the onset of...recovery...Australia’s structural reforms have been in advance of those in many other OECD economies” (Filmer & Dao, 1994, p. 43).

²⁷⁸ For Keating, re-election on 13 March 1993 was “the sweetest victory of all...a victory for the true believers...We have turned the corner, the growth is coming through. We will see ourselves as a sophisticated trading country in Asia.” Retrieved from <http://australianpolitics.com/1993/03/13/keating-sweetest-victory-true-believers-speech.html>.

Like Hawke, Keating was a staunch believer in the 'turn to Asia'.²⁷⁹ He believed wholeheartedly that Australia was destined to be a major player in Asia. He made many seemingly anti-British remarks and was a defender of Australian republicanism.

I always thought Australia could be a great country but it had to have a different idea of itself. That is, an efficient, competitive, open, cosmopolitan, republic integrating itself with the Asian region. I'd given the country a new economic engine so what I wanted to do as PM was repoint the raft to the area of opportunity and our ultimate security, which was Asia...That was the approach I took and that really governs the whole prime ministership (P. Keating, 2013, p. Ep.4 3:15).

A very symbolic gesture to this effect was Keating's repeated statement that that he will never go to Gallipoli (site in Turkey of a major losing battle for ANZAC soldiers in WWI), instead believing that the Kokoda Trail campaign in Papua New Guinea during WWII is more significant, since the opposing Japanese forces were considered a direct threat to Australia itself. Why focus all attention on a battle supposedly fought for Britain when Australians could honour a battle fought for its own survival? He emphatically demonstrated his feelings when, on an official visit to the island nation, he knelt and kissed the ground in the village that gives its name to the campaign.

Whilst these views are particularly personal to Keating himself, they do contribute to the narrative that he was cognizant of the growing social and economic interdependence between Australia and Asia, as evidenced by Australia's resource, manufacturing, and service sector exports. Keating stated emphatically that "we can live and prosper in the Asia-Pacific" (P. Keating, 1992, p. 43). An important aspect of this was APEC, which encouraged engagement between SE Asia, East Asia, and the USA. Keating stated that he thought he could get President Bill Clinton's

²⁷⁹ See P. Keating (2000); Watson (2003).

agreement on APEC's trade governance aspect considering Clinton had just won an election on the mantra that 'it's the economy, stupid'; "he couldn't quite resist the intellectual opportunity of APEC" (P. Keating, 2013, p. Ep.4 27:29). APEC's success was achieved by design: "in the eighties, we took hold of the rudder and set about an essential economic transformation which leaves us able to hold our own in Asia in the nineties" (P. Keating, 1992, p. 44). Another aspect of interdependence was Australia's relationship with Indonesia. Keating went to there for his first overseas visit because Indonesia "is in the first rank of Australia's priorities" (ibid., p. 45). He outlined the close ties between Australia and Indonesia, describing them as having a pattern of interdependence stretching back centuries. As such, they both had an interest in each other's economic success.

Australia, Keating said, had "taken up the challenge of economic reform...We have learned how to build a competitive economy, where until very recently we were less than competitive" (ibid., p. 52). As well, he told his Indonesian audience, "most Australians see Asia and the Pacific as holding the key to our future...We urge you not to think of Australia as the place it was twenty years ago....[but as] a partner in the dynamic new world of the Asia-Pacific region" (ibid., p. 54). Yet despite looking forward towards Asia, there is no doubting Keating's antagonism towards the forward-thinking SPC process. He had specifically and purposefully used it to highlight Hawke's weak leadership and denuding of Commonwealth powers. Why did Keating not kill the entire process? As his speech in Indonesia makes clear, what Keating did recognize was the achievement of significant reforms to improve Australia's competitiveness, which were a direct result of the SPC process. Rather than kill the entire process, Keating used it to further

his *One Nation* agenda to continue reforming Australia and achieve his vision of stronger and more persistent ties with Asia.

But that did not mean Keating had to like the SPCs. He reluctantly agreed with the Premiers that there was “value in regular discussions at HoG level”, but only if the name was changed from Council of the Federation, which “has come to be associated with the States’ specific proposal which we cannot accept” and lacked “recognition of the special position of the Commonwealth in the Federation”.²⁸⁰ His view was evident in the lead up to the final SPC in May 1992, when Keating was described as “bashing” the states in cabinet meetings: “they were being lambasted for not restraining their spending in the halcyon days of the 1980s, for which indiscipline they were now suffering” despite *One Nation’s* spending on infrastructure (Blewett, 1999, p. 109). The stimulus spending did seem to make the May summit less difficult, Keating admitted after, with Greiner supporting him despite political trouble for the governing Liberals in NSW; Keating said of Greiner that he is “policy sensible” (ibid., p. 112). Policy mattered more to Keating than anything else in government except perhaps becoming PM; “[he] guarded his energy by focusing on substance and neglecting procedure” (J. Edwards, 1996, p. 466). His attention to policy details rather than the negotiations themselves was in stark contrast to Hawke’s leadership style. Hawke was a conciliator and revelled in finding agreement whilst Keating was more adversarial and abrasive (Painter, 1998a). Not for the first time would leadership style thwart efforts at cooperative federalism.

The SPCs were about both policy and process. Neglecting the process risked the achievement of substantive policy reform. In the end, it did not matter since Keating “profoundly

²⁸⁰ FOI request, DPMC (FOI-14-035), “Meetings of Heads of Government: Talking Points,” [no date], p.3.

disagreed with the objectives of [the SPC]". He agreed to form COAG only in return for "agreements on national electricity, gas, rail and water cooperation...But he would not allow negotiation of changing the distribution of tax powers" (J. Edwards, 1996, p. 471). Such issues were already discussed at "annual financial Premiers Conference and Loan Council meetings [and] the Commonwealth could not accept that it must submit all proposals for new Tied Grants to HoG for approval".²⁸¹ For Keating, the Commonwealth's spending power was "the glue that holds the federation together" (quoted in Painter, 1998a, p. 18), and COAG would never replace it. Nevertheless, agreement was reached. The communiqué after the May summit elucidated a charter for COAG, which stated its intention to increase cooperation in areas of national interest, the economic union, and the functioning of the federation. As well, all HoG signed a mutual recognition agreement, with NSW passing the first enacting legislation by December.²⁸²

Gone were the days when the SPC process embraced the whole range of issues, when Commonwealth and states were prepared to make big changes to the Australian economy and to the operation of its federal system. The latter issue had now been jettisoned. The states managed to reform IGR but fiscal federalism would have to wait. It was not only Keating's fault. Some states were becoming reluctant to reform. Under a new Premier facing an uphill battle for re-election, SA was concerned that "through micro-economic reform,...SA interests may be endangered: aggregate national economic efficiency may well be maximised by concentrating infrastructure investment and coordinating authority in the eastern States" (Parkin & Marshall, 1992, p. 120). It was clear that by May 1992 the window of opportunity for radical change was

²⁸¹ Ibid., p.2.

²⁸² See Wright (1993) for an overview of mutual recognition. She argues that it weakens state sovereignty.

closing;²⁸³ IGR reform barely squeaked through. From Hawke's point of view, "Paul Keating's use of the issue in his campaign to destabilise my leadership denied Australia the benefits which could have come from a full continuation of the New Federalism initiative" (Hawke, 1994, p. 531). Yet COAG was founded and continues to operate to this day.

In terms of its level of institutionalization, COAG was founded at a medium level of institutionalization whereas its predecessor, the annual Premiers' Conferences, were weakly institutionalized. The changes emanating from the SPC process are palpable. Whilst Premiers' Conferences had regularity since they were held annually, the density of contacts between officials was paltry, with states receiving the Commonwealth offer under the hotel door hours before the conference. There was no secretariat, the Commonwealth dominated decision-making, and the conference agenda contained only one issue: the budget.

Contrast this to the SPC summits outlined above. The density of contact between officials increased greatly as evidenced by the preparatory work conducted before each summit. Even though COAG was not founded with a secretariat, within the DPMC a steering committee was organized to coordinate meeting preparation, which continues to operate. It is controlled by the PM but its coordination with the states is a significant improvement on the annual Premiers' Conferences. Finally, it must be noted that SPCs had characteristics of strong institutionalization, particularly the fact that the mutual recognition agreement became law at both the state and Commonwealth levels. With an increase in COAG's independence via supporting institutions as well as a move away from consensus decision-making, COAG has the potential to become a strongly institutionalized body within the Australian federation.

²⁸³ D. Brown (2002) refers to this as 'reform fatigue'.

Key officials responsible for the preparation of COAG meetings within the Commonwealth and state governments indicated in interviews that COAG is an important element of Australian IGR; they infused it with value. It is valued for its ability to allow HoG to caucus and to facilitate cooperation between states. For the more influential states, there is the question on what issues do they want to spend their political capital vis-à-vis the other states, particularly in getting the other larger states to agree.²⁸⁴ States have the right to put items on the agenda, but the major issues of the day will take precedence; COAG is topical and current. Officials noted however that “it doesn’t work when the Commonwealth exercises its fiscal muscle. If the players were more even, if they were equals, then no unilateral action would be possible, otherwise the Commonwealth prevails”.²⁸⁵ As well, agreements that are not entered into law have a different status. COAG should enforce these agreements, officials noted, but at times it is not a staunch defender of IGR since it is dependent on the “power and gumption of the PM”.²⁸⁶ Officials agreed that COAG is suitable to the discussion of issues but that agreement is not always forthcoming. Its advantage is that it keeps long-term issues on the agenda, which benefits the smaller states with their more specific issues.²⁸⁷ In all, the evidence is that COAG is most certainly institutionalized with Australian IGR, but that its promotion to a stronger level is not likely in the near future, at least not without another window of opportunity.²⁸⁸

²⁸⁴ Interview with NSW DPC, 19 June 2014.

²⁸⁵ Interview with QLD DPC, 30 June 2014.

²⁸⁶ Ibid.

²⁸⁷ Interview with WA DPC, 21 July 2014.

²⁸⁸ An example of how not to open a window of opportunity was the recent proposal by PM Malcolm Turnbull to allow states to raise income taxes for the first time since WWII (see Grattan, 2016). It is a proposal that the states wanted back in 1991 but one that Hawke could not accept. When the states finally had it on the table at the April 2016 COAG meeting, they rejected the deal based on how it was proposed.

Conclusion

The reasons for launching the SPC process and for its institutionalization are separate but linked issues. The above has woven the different reasons into one single tapestry, demonstrating the complexity involved in understanding HoG decision-making, intergovernmental relations, and economic reform. Despite the peculiarities of the Australian case, it is possible to discern the key variables that determined COAG's institutionalization and to understand which of those are generalizable to like cases.

It is clear that the SPCs were borne directly out of an economic crisis and the political response to it. M. Edwards and Henderson (1995, p. 34) describe COAG as a response to the "faster tempo of global economic integration". The key macro-economic indicator was the current account deficit. The Commonwealth's determination – Keating's in particular – to eliminate the imbalance was where the economic environment most directly transmitted signals to the political realm. Inflation and unemployment were important too but these were directly affected by the current account deficit, which was a product of the many shifts occurring in the Australian economy: the declining price of commodities, Australia's failure to participate in expanding world trade (with manufactures overtaking commodities), the reorientation of Australian trade towards Asia, and internationalization's exposure of an uncompetitive, overregulated, and inefficient domestic market. These shifts had a profound influence on policy-makers, convincing them that restructuring and internationalizing the economy were necessary if Australia was to continue prospering.²⁸⁹

²⁸⁹ See McLean (2012).

At the Commonwealth level, macro-economic reforms were handled first, in particular curbing wage inflation, floating the dollar, and deregulating financial services. These reforms were largely elite-driven and were underpinned by the government's Accord with the trade unions and employers.²⁹⁰ The goals of restructuring and internationalization also influenced foreign trade policy, with the most significant changes occurring to export promotion, tariff rates, and the creation of both the Cairns group and APEC to respond directly to the 'turn to Asia'. When all these initiatives partially failed²⁹¹ to alleviate the imbalances, policy-makers pushed onwards with reform, adding austerity budgeting and microeconomic reform.²⁹²

Some of the states, notably SA and NSW, were already implementing reforms. With a recession underway, and the reform agenda focused squarely on the budgetary and competitive advantages of microeconomic reform, key actors within both orders of government concluded that a coordinated economic reform effort was required if their independent efforts were to alleviate the recession in the short-term and complete a fundamental economic restructuring in the long-term. Addressing these issues was crucial if Australia's states were going to successfully manage the 'turn to Asia'. Bannon in particular recognized in 1986 that Commonwealth-state cooperation was necessary to achieve progress on one of the key reform issues, duplication and overlap, and Mike Codd had approached the PM after the 1987 election with a proposal for enhancing coordination. The critical juncture that scheduled the actual summit was the dust-up at the June 1990 Premiers' Conference.

²⁹⁰ See Gruen and Shrestha (2000).

²⁹¹ See P. Forsyth (1992).

²⁹² See R. G. Gregory (1992).

The usual fight over the budget at the annual Premiers' Conference was not enough in the past to begin a process of IGR reform – Premier Cain noted strained relations at the 1987 Premiers' Conferences, which is but one example of what little value these conferences engendered. To understand why the 1990 Premiers' Conference dust-up occurred and helped launch the SPC process, it is necessary to understand its context. Restructuring the Australian macro-economy had directly exposed the IGR system to external pressures for change. Exposure was in the form of tariff cuts, which Garnaut stated should occur more swiftly in order to capitalize on the 'turn to Asia,' a recommendation which Hawke subsequently used during his last re-election campaign. Then at the 1990 Premiers' Conference, actors were forced to confront the reality that governments were incapable of independently completing Australia's internationalization and righting its imbalances. States were feeling the squeeze both fiscally and economically, which forced them to directly and vocally confront Canberra's policy agenda. The result was a new commitment from both orders of government to cooperate. Centralized fiscal federalism and a relatively high VFI may have required a small degree of routinization of Premiers' Conferences but fiscal federalism alone cannot explain why cooperation was further institutionalized in 1992. Other inducements were necessary to launch the SPC process and raise the level of summits' institutionalization.

Australia's arm's length federalism had biased the Commonwealth's first wave of reforms;²⁹³ either it acted alone or through its fiscal dominance. Yet the Commonwealth's fiscal capacity and macro-economic jurisdiction never eliminated the constitution's concurrency in policy-making. Rather, the constitution proved flexible enough to allow solutions to emerge, one

²⁹³ See Carroll and Head (2009).

of which was the SPC process. However, even when the centralist bias was overcome, the institutionalization of COAG was not guaranteed. What was required still was a certain process of reform, one that is born out of reforming the economic union, a process that touches many different policy areas, requires many rounds of negotiation to achieve meaningful and substantial progress, and invariably involves leaders crafting package deals to overcome special and regional interests and the limitations of political capital. Package deals are political choices amongst a host of technical policy choices, for which HoG are uniquely positioned to craft because of their democratic legitimacy and authority. All of these characteristics are evident in the mechanism of continuous negotiation. Continuous negotiation on economic policy locked leaders into a routine of strategic and political decision-making across all policy areas, which invariably included IGR institutional change. Thus, Hawke's proposal to launch a *series* of SPCs to engage a second wave of reform coupled with his genuine commitment to fiscal reform produced the necessary framework for IGR institutional change in the form of more routinization and an infusion of value. A series of HoG summits was the correct response to the goal of economic and fiscal reform; the yearly Premiers' Conferences and the Ministerial Councils were all inadequate to the task.

As the mechanism of continuous negotiations engaged, leaders came to recognize the value of institutional reform in order to achieve their economic reform goals. Ken Baxter (2014) recalled that "PMs Hawke and Keating and Premiers Greiner, Goss and Kennett recognized the world had changed and Australia had to behave as a single nation – not a motley collection of State based fiefdoms". A changing world economy impacted and radically altered Australia's political economy. The shift from concentrated external market integration to diffused – i.e., the 'turn to Asia' – produced an incentive for actors to cooperate on internationalizing and

liberalizing the Australian economy in order to increase its competitiveness and take advantage of the opportunities from the emerging Asian economies. Once committed to reform, the solution to the competitiveness issue – implementing mutual recognition and tackling duplication and overlap – forced actors to take a hard look at their IGR system, which was eventually reformed as well.

Actors' commitment to their reform process manifested in dramatic fashion when Premiers held their own summit after the Commonwealth momentarily abandoned its seat at the table. The Premiers-only summit in Adelaide reinforced the process and convinced actors that institutionalizing a permanent IGR decision-making body inclusive of all orders of government was the only way to achieve and sustain real change. The Adelaide summit was not a snub to the Commonwealth, it was a strong show of support for Hawke's reform process (Bannon, 1992); Premiers were willing to go it alone to complete the process. The Premiers' direct appeals to Hawke after the summit and their proposal to found COAG demonstrate the reliance of IGR institutional change on a process of economic reform.

Thus, the Australian case demonstrates the workability of the theory of HoG summit institutionalization in other multi-level systems. Securing the commitment of sub-units required engaging them on a range of policy issues that could address their vulnerabilities to the shifting external trade structure. The need for intergovernmental negotiations and HoG involvement in the reform process produced the mechanism of continuous negotiation. Once engaged, an opportunity was created for actors to be influenced by various incentives, some electoral, others institutional, and still others emanating from the political economy. The incentive to cooperate generated by the 'turn to Asia' and the economic crisis impacted the mechanism such that

leaders, seeking a successful outcome to their reform process, called for changes to their process of intergovernmental decision-making.

The story of economic vulnerability emanating from the 'turn to Asia' is incomplete however without appealing to the leadership variable. Shifting economic fundamentals may have exposed the IGR system to external pressures but it was political leadership that determined the results; the former may have opened the window of opportunity but it was the leaders themselves who had to step through it. As Sturgess commented in December 1992, microeconomic reform has a desperate need for leadership: "the scarce resource is people, good people, people who can lead" (Sturgess, 1993, p. 14). It is clear that without Hawke and Greiner, a coordinated economic reform process would have been more difficult to begin and may never have led to a series of cooperative summits that would convince HoG to institutionalize them. The key leader in any reform process would always have been the PM by virtue of the Commonwealth's position as the central and dominant actor. Keating certainly felt that way: "The public will never understand the value they got out of Hawke and me...The changes were revolutionary. I would kick and shove and gouge and he would sort of do the same. But nevertheless both of us had our eye on...the greater public good of the place" (P. Keating, 2013, p. Ep.2 51:04). Yet other PMs tried to reform federalism and failed.²⁹⁴ Such facts reveal that the leadership variable is a double-edged sword. Whilst pivotal to success in IGR fora, it also means that IGR is "managed through actors and relationships, which are subject to churn" (Menzies, 2013, p. 383). The churn forces scholars to pay close attention to HoG. So why did Hawke's particular effort succeed?

²⁹⁴ See Fletcher and Walsh (1991).

The economic crisis and ‘turn to Asia’ clearly exposed the weaknesses of Australian IGR. There is also little doubt that Hawke’s personality and model of leadership were key.²⁹⁵ As a former union leader, Hawke considered cooperation and consensus as central elements of his decision-making. Yet he also thrived on conflict. Rancorous Premiers’ Conferences and the ongoing recession required a trouble-shooter to bring all the parties together to launch a concerted reform agenda. It helped that Hawke’s extraordinary political success was in part due to his relationship with the Australian people.²⁹⁶

Hawke’s effort, whilst bold and extraordinary, would have amounted to nothing if not for the leadership of key state Premiers. Greiner’s belief in apartisan policy-making – in getting the job done – ushered him through the window as well. His credibility as a reformer was in place before the SPCs began and was bolstered by the fact that he was the only Liberal HoG. Coming to an agreement with a Labor PM and group of Labor state Premiers was extraordinary and is further evidence of the power and influence that the ‘turn to Asia’ had on Australian politics. Sturgess commented that “in a very real sense, [the Premiers] functioned as a cabinet over those eighteen months” (Sturgess, 1993, p. 8) despite their partisan affiliations. Carroll and Head (2009) note the linkages established between state governments as a result of the SPC process. Greiner’s leadership helped translate Hawke’s message for ‘closer partnership’ into a call to action from the state Premiers themselves.

Yet Hawke’s qualities were also his undoing. His steadfast refusal to move off the stage in favour of Keating despite his promise to do so contributed to the near-demise of the SPC process.

²⁹⁵ See Bramston (2003).

²⁹⁶ See Mills (1993).

Keating's use of the process to sabotage Hawke's leadership and win the support of the Labor caucus would not have been possible if not for Hawke's view of himself as "Chairman of the Board of Australia Unlimited – essentially above parties, above industry, the supreme national authority" (Mills, 1993, p. 5). The entire initiative was tied so closely to him that it too was left vulnerable: "The process was unambiguously Hawke's – only Hawke, with his negotiating skills, patience and eye for detail could have carried it off" (ibid., p. 259). Partly this is due to the fact that many times throughout Hawke's term in office he and Keating pursued policies that were "traumatic for the party and the caucus" (Bramston, 2003, p. 65). Only Hawke's charm and electoral wins – and Keating's policy competence – brought them along. When the final moment arrived to seal a deal with the states, Hawke was no longer leader. COAG was institutionalized as part of a smaller deal on Keating's microeconomic reforms. The fact that it was institutionalized even after this near-death experience testifies to the impact that cooperative summits, political leadership, and the political economy can have on infusing an institution with value. The infusion occurred, but not completely. As Hollander and Patapan (2007, p. 281) conclude, "pragmatic federalism...has incidentally favoured the Commonwealth at the expense of the states" due to the failure to reform the VFI in the early-1990s. As well, the Industry Commission (1994, p. 30) concluded in October 1994 that the states were reluctant to press ahead with further competition reforms because they were trying to protect their dividends and tax revenues. It did not have to be this way.

From 1992 onwards, Australia experienced unprecedented economic growth. Keating said that he would take his mistakes – "the recession we had to have" quip being a big one – so long as he could also "live with the 22 years of growth and low inflation that followed" (P. Keating,

2013, p. Ep.3 42:41). Growth occurred and it did so under the auspices of a reformed federal system. Australia's leaders created a peak intergovernmental body whose cooperative element went on to counterbalance the conflict that had previously characterized Australian federalism.²⁹⁷ Conflict did not disappear (the Premiers again staged a walkout at the 1994 COAG meeting) yet neither did cooperation, which COAG managed to sustain (VFI reform was achieved somewhat in 2000 when the GST was created).²⁹⁸

The leadership variable is the least translatable to other political systems. The most that can be said is that students of federalism must recognize explicitly that IGR is about a small and special group of people. Their relationships and the processes they conjointly operate matter significantly. COAG was a product of Hawke, Keating, Greiner, Bannon and the others as they reacted to the overwhelming changes occurring to the Australian political economy. When certain political weaknesses are exposed by economic pressures, change itself is not guaranteed and neither is a specific outcome. All the political economy incentives in the world may not overcome intransigence and uncooperative attitudes. Leaders are responsible for interpreting the signals and setting the policy agenda. In short, cooperative federalism needs leadership to action the incentive to cooperate. The key point is that leaders – once they are convinced or forced to launch a reform process – will find that they have a greater chance of reforming institutions if such reform is accompanied by meaningful and broadly-based economic reform.

²⁹⁷ Hollander (2006) argues that COAG and National Competition Policy have left a legacy of a stronger centre.

²⁹⁸ See Morris (2002). COAG also managed to sustain microeconomic reform, see Filmer and Dao (1994); Painter (1998b).

PART THREE:

CANADIAN FIRST MINISTERS' CONFERENCES

Chapter 5:

The Other Lucky Country and the AIT

"[The AIT is] a pragmatic document that reflects the kind of compromises required to keep the unwieldy Canadian federation wheezing along".

Toronto Star editorial, 2 July 1994

Why, in contrast to the Australian experience, were Canadian First Ministers' Conferences (FMCs) not institutionalized as the peak decision-making body of Canadian IGR? Through the Canadian lens, it would seem Canada's defunct FMCs appear to be the result of its particular federal attributes; i.e. weak party integration, provincial demographics, and a small vertical fiscal imbalance. Yet when more carefully compared to the Australian experience, it becomes apparent that the political economy affects the operation of the IGR system.

Global economic forces had a major impact on both Australia and Canada in the 1980s and 1990s. Australia's economic crisis and 'turn to Asia' – the shift from concentrated to diffuse external market integration – produced an incentive to cooperate that impacted the mechanism of continuous negotiation on microeconomic reform and expanded those negotiations to include IGR system reform, which founded the Council of Australian Governments (COAG). In Canada, the Agreement on Internal Trade (AIT) represents a similar moment of continuous negotiation on microeconomic reform yet it did not lead to the institutionalization of FMCs. Why is this the case? This chapter emphasizes Canada's economic structure and international position in comparative perspective. The direction of change was influenced by Canada's political economy, which is sufficiently different from Australia's that it prevented rather than encouraged HoG summit institutionalization.

Canada, like Australia, is a mixed economy – developed but semi-peripheral – that faced the same challenges posed by internationalization and liberalization. By the late-1980s, policy-makers were faced with a deteriorating economic situation owing to declining productivity and competitiveness, which mirrored the economic crisis faced by Australia at the same time. Reforming internal trade was seen as one response to these problems, as was the ongoing debate

over free trade with the USA. To complicate matters, this story of economic reform is intertwined with the era of mega-constitutional politics. As politicians grappled with these issues, proposals for the new and improved governance of the economic union were considered, watered down, and ultimately failed to find expression in the constitutional accords. Policy-makers then had little choice but to turn to their governments' intergovernmental capacity to manage the economy. The AIT is therefore a product of two moving parts, one political, the other economic. The failure to improve the governance of the economic union via constitutional amendment placed a heavy burden on the competitive IGR system.

Once all Canadian heads-of-government (HoG) decided to reform the internal market, negotiations began in earnest to determine the AIT's mandate and overall structure, i.e., whether it should be a comprehensive deal based on general principles affecting all trade or a series of smaller sectoral deals. The federal government argued that a comprehensive agreement was required to deal with other issues, such as regional development, competitiveness, and international free trade. At that moment in the early-1990s, Canada appeared ready for its own 'closer partnership' moment, with Ottawa proposing economic and fiscal reforms in collaboration with the provinces, a process the Australian case demonstrates has the potential to institutionalize HoG summits.

The chapter begins by reviewing current debates in the Canadian IGR literature, establishing the need for institutionalized FMCs, and highlighting the similarities between Australian and Canadian HoG summitry. It is followed by an overview of the Canadian economy and the crisis that emerged in the 1980s and 1990s. Efforts at reforming the economy are then reviewed in the third section, which is divided up to discuss the failed constitutional negotiations

and the subsequent shift to the intergovernmental negotiations that proceeded the decision in 1993 to begin formal negotiations on the AIT.

Literature Review on Canadian FMCs

Canada has lived with IGR between the orders of government since Confederation, and with FMCs since the turn of the last century. Canada was in fact destined to have institutionalization owing to the rise of executive federalism, the development of collaborative federalism, and an increase in IGR activity at and below the ministerial level. Yet FMCs remained weakly institutionalized, except perhaps during the era of mega-constitutional politics, when leaders met regularly. After the early-1990s, FMCs resumed their weakly institutionalized state. The following literature review examines the arguments for institutionalized FMCs in Canada and explores the debate on what influences the overall IGR system. Some scholars point to the dependence of FMCs on partisanship and leaders' personalities whilst others point to the influence of external pressures. As of yet, an analysis has not been produced on the effect of the political economy on FMCs and how it interacts with the partisanship and personality variables. The dissertation seeks to address this gap in the literature.

There is no question that the value of FMCs plummeted after the failure to ratify the Charlottetown Accord in 1992, particularly since the continuation of the Regina Accord depended on its ratification. During the 1984 election campaign, Brian Mulroney promised he would "end parallel or incompatible planning once and for all between the two orders of government....with the 11 [HoG] themselves working together in an appropriate institutional framework advising as to the options envisaged and the directions to take" (quoted in Papillon & Simeon, 2004, p. 212).

The result was the 1985 Regina Accord, which established a framework for the Annual Conference of First Ministers (Simeon, 1988). Efforts to restart FMCs after the 1992 referendum failed. The era of mega-constitutional politics changed and then completely reversed the nature of FMCs, from quasi-institutionalized body under the Regina Accord to an informal mechanism “designed to deal with pressing issues...rather than a forum for on-going cooperation, as the logic of collaborative federalism would dictate” (Papillon & Simeon, 2004, p. 115). FMCs fail to occupy the apex of the federation’s decision-making process – they have proved incapable of driving the rest of the political system – leaving policy-making to each order of government independently or to the lower levels of the IGR system. FMCs remain ad hoc and sporadic and are often motivated by political ends detached from any meaningful management of interdependence over the longer term. Agreements reached at FMCs generally lack specifics and have no legal basis. FMCs are not routinized and have limited value, and are therefore weakly institutionalized (Bolleyer, 2006).

The evidence for weakly institutionalized FMCs is found in the number of meetings held before and after the era of mega-constitutional politics. After the Charlottetown Accord referendum, FMCs were held infrequently, with just nine meetings convened in the 20 years since 1992. This compares with 29 meetings in the 20-year period leading up the referendum (Canadian Intergovernmental Conference Secretariat, 2004). These pre-referendum meetings are in fact an illusion of institutionalization. Between PM Mulroney’s first FMC in 1985 and the 1992 referendum, six out of fourteen meetings were held on constitutional matters. Four FMCs were convened just on the economy (and three of these were mere FMMs not FMCs) whilst the

other four were annual conferences of the HoG.²⁹⁹ PM Harper convened a full FMC only once during his nine-year tenure and he refused to attend CoF meetings. How PM Trudeau will operate is still unclear, although pundits have begun speculating that a low confrontation, high consultation, ‘hug-it-out’ approach is emerging (e.g., Wells, 2016).

These developments over time reflect a significant characteristic of FMCs: “governments...make the fundamental choices to agree or disagree” (Dupré, 1985, p. 1). In other words, the workability of Canadian federalism rests on whether “[a FMC] provides a forum...that is conducive, and perceived to be conducive...to negotiation, consultation or simply an exchange of information.” The success of FMCs depends on high levels of trust among participants and on whether or not norms are internalized (David Cameron & Simeon, 2002). Because of a lack of trust and institutionalization, Papillon and Simeon (2004) describe FMCs as the weakest link in Canadian federalism.

Despite the contemporary history of FMCs, recommendations for their institutionalization pervade the academic literature. Starting with Dupré (1985), such calls emanate from an understanding of executive federalism, which is a product of the policy interdependence and political independence of Canadian governments (Smiley, 1987). Papillon and Simeon (2004) conclude that FMCs are essential because they double as both a forum for collaboration and for the expression and accommodation of regional differences. David Cameron and Simeon (2002) point out that it is a mix of interdependence and independence that leads to collaborative federalism, in which broad national policies are co-determined by both orders of

²⁹⁹ See Canadian Intergovernmental Conference Secretariat (2004) for a list of the topics and attendees of HoG summits in Canada since 1906.

government. They conclude that collaboration has become part of the ‘federal condition’ of Canada (see Smiley, 1987). Hale (2004) argues that collaborative federalism’s success depends on bilateral or ‘checkerboard federalism,’ itself a result of the functional specialization in Canadian IGR and economy emanating from North American integration. Some authors go even further, arguing that such integration constitutes a ‘supra-constitutional’ restraint on policy-making (see Grinspun & Shamsie, 2007).

The federal condition of Canada is now more important than ever given Canada’s economic challenges. The condition and the challenges require institutionalized FMCs, which could facilitate coordinated strategic decision-making to effect the country’s adaptation to global economic shifts. Yet recent experience shows generally fragmented and decentralized decision-making across the IGR system, in which the institutions of collaborative/cooperative federalism have only weakly materialized. According to Hale (2004, p. 500), “the enormous range and diversity of Canadian intergovernmental and cross-border relationships...makes it more difficult for governments to coordinate the full range of their intergovernmental activities”. The lack of institutionalized FMCs results in the paradox of IGR in Canada: the dual existence of competitive and collaborative federalism.

Several scholars have noted the remarkable resiliency of Canadian IGR to change, even from the pressures of globalization (Hale, 2004; Simeon, 2003). Canadian IGR is seen to be characterized by continuity; a study that compared the situation in 1960 to the one in 2006 found the only notable change to be that various ministerial councils have slightly institutionalized, i.e., meetings are held more regularly with formal decision-making rules (Simeon, 2006). The observed resiliency of Canadian IGR to change requires scholars to understand why this is the

case. If institutionalized FMCs are the logical conclusion of the federal condition of Canada and the need to adapt to changing world economic conditions, then what factors determine its level of institutionalization?

Papillon and Simeon see FMCs as dependent on the nature of Canadian parliamentary federalism, the political needs of governments, and even on the personalities of HoG. That is, FMCs are not a strong independent variable that shapes the political system. Rather, they are dependent: “its role, character, and effectiveness at any given time reflect forces and pressures coming from outside the FMC process itself” (Papillon & Simeon, 2004, p. 126). Simeon (2006) notes that Canadian IGR is impacted by provincial interests as well as the particular ideology, status goals, and electoral position of governments.

According to Simeon, weakly institutionalized FMCs are the result of Canada’s cultural setting, its institutional and constitutional framework, and the goals, attitudes and behaviours of leaders. Dupré (1985, p. 233) argued that executive federalism as a whole is “a function of the manner in which the executives...operate”, that is, in the relationship between bureaucrats and elected officials. Today’s concentration of power in the hands of the executive, specifically the PMO and Premiers’ offices (see Savoie, 2010), suggests that it is largely the personalities and priorities of HoG that determine the characteristics of FMCs.³⁰⁰

The Canadian literature has concluded that weakly institutionalized FMCs are a result of the 19th century institutional structure of Canadian federalism as well as on the partisanship and

³⁰⁰ Prime Minister Lester Pearson was a compromiser and accepted asymmetry whilst Pierre Trudeau wanted to reverse this trend. Jean Chrétien remained suspicious of provincialism and collaborative decision-making. Paul Martin had more of Pearson’s instincts as a compromiser but his asymmetry perhaps went too far (Simeon, 2006). And Stephen Harper touted open federalism: the retreat of federal policy making from areas of provincial jurisdiction (see Mendes, 2012).

personality of leaders. The result is an uneasy federation in the 21st century, which Brock (2003) has labeled as 'beggar-thy-neighbour'. Such federal-provincial wrangling has led to the paradox that Canadian IGR is collaborative yet disentangled (Bolleyer, 2009). Indeed, by the mid-1990s, both orders of government shied away from formal IGR at the HoG level, convening FMMs rather than FMCs (Papillon & Simeon, 2004, p. 128).³⁰¹ The barrier to institutionalization, according to Bolleyer, is the majoritarian dynamic of both orders of government. Conflict over policy and money shapes the tactics of actors, producing a system too feeble to support any process of formalized and sustained coordination. Bolleyer and Simeon both conclude that actors drive IGR, that it is personalized rather than institutionalized. More recent developments are indicative of more cooperation at least at the provincial level through the Annual Premiers' Conference, now called the Council of the Federation.³⁰²

Notwithstanding the mega-constitutional negotiations, Canadian and Australian HoG summits are remarkably similar. Both remained weakly institutionalized into the late-1980s, both were characterized by informality and competitive relations between orders of government, and the effectiveness of both were seriously questioned, particularly the ability of HoG to make decisions and coordinate policy. Finally, both institutions managed to produce spectacular failures – the 1990 Premiers' Conference dust up in Australia and the failed constitutional negotiations in Canada.

³⁰¹ FMMs are essentially less-politically sensitive FMCs; they provide HoG with political distance from constitutional issues by distinguishing them as single-issue meetings, such as on the economy or health care.

³⁰² The CoF has become part of the IGR process, especially in its attempts to engage the federal government, see Adam (2005); Meekison (2004). Even when FMCs were moribund, CoF meetings continued to call for federal participation.

In Canada, questions surfaced regarding the effectiveness of institutionalization (J. Simmons, 2004), which originated from the idea that ambiguity rather than formality is the key to achieving cooperation given Canada's federal condition and its resulting paradoxes (A.-G. Gagnon & Erk, 2001). Simmons's analysis demonstrates that stronger institutionalization does not necessarily result in compromise or consensus decision-making. She then asks why cooperation occurs in the first place and why it varies across policy sectors. The conclusion is that Cameron and Simeon were correct; collaboration is alive and well in Canada but that variance is due to 1) external pressures, such as scrutiny from environmental groups; 2) ministerial and sectoral actors, who are in constant communication and share common norms and values; and 3) the policy's political salience with the electorate.

The idea that IGR is impacted by external pressures was adeptly discussed by Courchene (1991, 1995). In this analysis, globalization causes power to erode away from the state upward to supra-national institutions and downward to local authorities. Courchene referred to this process as 'glocalization' and argued that the IGR system, particularly FMCs, must respond to these shifting power dynamics between orders of government. From Hueglin's (1990) perspective, the effects of globalization on business interests will reduce federalism's capability as an independent variable to shape politics and economics. Rather, federalism will either alleviate the conflicts engendered by globalization or worsen them. Hale and Kukucha (2006, p. 181) ask "why has a coherent policy regime based on federal-provincial collaboration emerged in trade policy and not in financial services or capital market policies to promote increased levels of investment in Canada?"³⁰³ Their investigation reveals that international trade regimes were

³⁰³ Note their study focused on a specific and technical policy sector rather than FMCs, which deal with all policies.

responsible for the creation of the AIT and also CTRADE, the federal-provincial committee system for international trade negotiations.³⁰⁴ As for the investment and capital policy areas, the authors conclude that no national regime for cooperative policy-making exists – despite repeated reports advocating for harmonization – because of an absence of an international legal framework for these areas (ibid., p. 204). To further the point, Anastakis (2009) investigates the auto industry and finds that once free trade between the US and Canada was engaged in this sector, Ottawa-Toronto relations changed from conflict-ridden to one of cooperation.

The main point of these studies is that the structure of the international economic environment impacts elements of the IGR system. These stand in contrast with the viewpoint that FMCs are unlikely to change as a result of external pressures because the IGR system is able to “generate effective policy that balances the competing identities and interests which are Canada’s enduring legacy” (Simeon, 2006, p. 331). Thus the literature leaves us with an unresolved debate: are FMCs dependent on the partisanship and personality of leaders or are they impacted by external pressures? The answer is most certainly a combination of factors. However, those who agree with Courchene’s premise – that FMCs are directly impacted by outside forces – have not produced a comprehensive account of how the political economy impacts such meetings, resulting in an over-emphasis on factors such as partisanship and fiscal relations.

³⁰⁴ See Skogstad (2012) and Muirhead (2009). The impact of international trade negotiations on IGR is not being compared here because international trade negotiations are contained within themselves, whereas the AIT, and its inclusion of multiple policy areas, was a more broadly-based reform with the potential to expand to many if not all areas of domestic economic and social policies involving areas of intense public scrutiny and therefore more likely to include the HoG and lead to substantial IGR institutional reform.

Brown's exhaustive study of economic union reform in both Canada and Australia goes some way to uncovering specific reasons for why change to IGR institutions occurs. For D. Brown (2002, p. 261), IGR's effectiveness relies on a diverse set of policy tools. The tool kit includes 1) regulatory options, such as mutual recognition or harmonization, 2) decision-making procedures, such as unanimity or majority voting, and 3) institutional structures, such as sub-unit-only cooperation or federal government involvement. Australia and the EU have been more successful at encouraging IGR cooperation using this tool kit, but Canada too has achieved some success. Both Australia and Canada adapted to globalization by engaging in a collaborative reform process with institutions more suited for competitive federalism. He argues that intergovernmental agreement – the third option for reform after unilateral federal action and constitutional agreement – was more successful owing to comprehensive agendas and windows of opportunity. Federalism is “alive and well” in Australia and Canada; both showed a capacity to adapt to globalization whilst preserving federal values: “Recent Australian and Canadian experience demonstrates that intergovernmental cooperation is the best means to achieve economic union reform....[They] have demonstrated an improving capacity for intergovernmental co-decision...Therefore, more than just surviving, federal states can be ‘strong’ states in an era of globalization” (ibid., p. 265).

Brown explains that Canada's more diverse federal society and coordinate (separate) distribution of powers leads to a more competitive, low intensity IGR system that emphasizes provincial fiscal autonomy. Australia is more homogeneous and has a greater nation-building ethos, more concurrent powers, and centralized fiscal federalism. Yet the Australian case presented in the previous chapters demonstrates that whilst these elements did play a role in

COAG's institutionalization, they alone were insufficient to explain its creation. Thus, there is a piece missing in Brown's analysis, namely, the political economy.

What are the differences between Canada and Australia's political economies? Australia experiences diffuse market integration in its region, with many trade partners and low integration. Canada has concentrated market integration, owing to one dominant trade partner and the presence of institutions governing bilateral trade (ex. NAFTA). The result is that Australia experienced competition reform whilst Canada experienced free trade reform (ibid., p. 238). Yet Brown may have overstated these differences since Canada and Australia both considered domestic reform as the key to improved competitiveness and productivity. Internationalizing their economies involved bargaining and coordinated policy implementation between orders of government, which in turn required continuous negotiation across multiple policy areas. As well, Australia unilaterally cut tariffs, effectively ushering in free trade reforms.

The task of this chapter and the next is to understand how the mechanism of continuous negotiation was engaged in Canada and why it produced a result different than that which was observed in Australia. The literature reviewed above provided some reasons for why change occurs yet it remains incomplete. Why did microeconomic reform and the mechanism of continuous negotiation fail to institutionalize Canadian FMCs? Answering this question completes Brown's comparison of economic union reform efforts in Canada and Australia – by connecting the political economy to IGR system design – and sheds new light on the AIT's outcome that he and others (mis)predicted: that it was a new, more effective method of policy-making that would revolutionize Canadian IGR. This did not occur and it remains to be seen why the mechanism for institutionalizing HoG summits succeeded in one case and failed in the other.

The Economy of the 'Other' Lucky Country

As well as having similarly competitive IGR systems, Canada and Australia also have quite similar economies. The following demonstrates that both are in fact lucky countries in the economic sense as coined by Horne. Like Australia, Canada is rich in commodities and relies on resource extraction and trade to compete in the global marketplace. Its semi-peripheral status also means that it too was forced to adapt in the 1980s and 1990s to significant changes in the world economy. These changes resulted in Canada experiencing a sense of economic crisis, a perception that was markedly enhanced owing to its concurrence with the constitutional and FTA negotiations.

The structure and complexity of the Canadian economy is best summarized by three policy orientations: a national policy, a provincial/regional policy, and a liberal-continentalist policy (Leslie, 1987). The simultaneous existence of all three orientations explains a modern Canadian contradiction: the commitment to both international liberalization and the resilience of internal trade barriers (Berdahl, 2012). The following short history of the Canadian economy helps elucidate this contradiction.

The question of how to develop Canada – whether through domestic or international trade – has been a key issue for policy-makers since its colonization. At the time of Confederation, implementing a national policy orientation laid the foundation for both the regional/provincial and the liberal-continentalist policy orientations. The National Policy of 1879 imposed a tariff on imports, thereby using a policy of import substitution to develop and industrialize the

economy.³⁰⁵ The National Policy was designed to prevent continentalism, which challenges the economy and thus the very existence of Canada. The result was increased provincial economic specialization and interdependence (Stevenson, 2012, p. 22). Manufacturers established operations around the major central Canadian cities whilst the periphery focused on their particular resource advantages. Disagreements over national development policies produced long-lasting tensions between regions and encouraged provincial-led efforts at development. As tariffs were gradually eliminated in the post-war era, the reality of provincial specialization generated a regional reliance on the relatively closer American market, which increased pan-Canadian tensions.³⁰⁶ Chambers and Percy (1992, p. 5) reinforce this view with their study of the Western Canadian economy: “Trade with the international economy rather than with the rest of Canada is the major vehicle for capturing gains from specialization and scale”.

By the post-war era, east-west trade was being supplanted by north-south trade. Such change “inevitably had the effect of enhancing the powers of the provincial governments in relation to the federal, since it was provincial resources that were being exploited, [and it] tied them to markets and corporate headquarters located in the United States” (Thorburn, 1985, p. 23). In the 1960s, *Lament for a Nation* by George Grant questioned whether Canada, as a branch-plant of the USA economy, could remain independent: “The British connection has been a source of Canadian nationalism. The west-east pull of trade...provided a counter-thrust to the pull of continentalism” (G. Grant, 1980, p. 33). According to Grant, the post-war economic policies of

³⁰⁵ For example, the Canadian automotive sector is the direct result of a 35% tariff imposed on USA car imports and 30% on automotive parts (Melanson & Martin, 2010).

³⁰⁶ Stevenson (2012) contends that because of the rise of the service economy, regionalism is shifting towards an urban-rural dynamic rather than region versus region.

Canadian governments contained the premise “that the Canadian economy was part of the total resources of North America; that Canada was an undeveloped frontier within that total, and the capital necessary for the development would come largely from the United States” (ibid., p. 38). It seemed that loyalty went with the flow of trade, first to the UK, then the Empire, and now ever more so to the USA (ibid., p. 69). The consequences were weakened nationalism and tensions between regions owing to their different economic structures (resource-based vs. industrial). For Rocher and Rouillard (2002, p. 227), economic integration of these different regions could only come at the cost of federalism itself. Gilpin (1972) recognized that American investment intensified the competition between English and French Canada as Ottawa sought to reduce its reliance on the USA whilst Quebec City encouraged American investment.

Innis argued as part of a theory of rigidities that Canada was an advanced industrial society reliant on its semi-peripheral status (Drache, 1991, p. 23). Development of resources, whilst capital intensive, requires that same capital to revert back to the centre and so resource exploitation fails to properly develop the periphery. It is essentially Horne’s argument: that relying on resource extraction and tariffs was a recipe for economic disaster. Canada, like Australia, has the attributes of a ‘lucky’ country; it is prosperous yet that success comes with the great risk of becoming “a rundown, old-fashioned, puzzled, and resentful [nation]” (Horne, 1998 (1964), p. xx).

All is not lost since “on the supply side the expansion of the export sector creates opportunities for domestic investment” to create linkages between industries (Watkins, 1991, p. 85). Creating these linkages and developing local economies require a well-functioning economic union to mitigate the effects of Canada’s semi-peripheral status and the provincial/regional

policy orientation. The economic union has many benefits, including its insurance and fiscal transfer aspects as well as its greater market power, particularly for an economy that is reliant on unstable commodity prices. The economic union is the glue that reinforces the country against the disintegrative forces of both the regional/provincial and liberal-continentalist policy orientations.³⁰⁷

Nevertheless, Grant lamented the weakening structure of the economic union: “The Liberal policy under [Minister C.D.] Howe was integration [into international capitalism] as fast as possible and at all costs” (G. Grant, 1980, p. 41). Grant sought to reveal the logical conclusion of Howe’s liberal-continentalism, which is that Canada has no reason to exist. Electricity was a major post-war culprit: “[it] contributed to the forging of stronger ties between the provinces and the United States because it increases dependence on the New York bond market for financing and, later, on the American market to sell the surplus” (Thorburn, 1985, p. 24). Further development of resources and investment in industries and infrastructure tightened these linkages and encouraged a regional/provincial policy orientation, complete with internal trade barriers as provinces favoured local businesses,³⁰⁸ thereby eroding the economic union by reducing competition, efficiency, productivity, and finally, the ability of the national market to prosper against the pull of continentalism.

The liberal-continentalist policy orientation also meant the curtailment of the interventionist practices of Canadian governments, a difficult task since “state interventionism has a powerful tradition behind it in Canada” (Leslie, 1987, p. 170). In fact, when the dollar was

³⁰⁷ Courchene (1995) argues that a ‘social policy railway’ was an even strong glue holding Canada together.

³⁰⁸ See Stevenson (2009).

allowed to float in the 1970s, the immediate response was more federal government intervention, including wage and price controls, higher taxes, foreign investment controls, and the National Energy Policy. This last effort at a national policy orientation was quickly discarded by the Mulroney Progressive Conservative government after 1984. The new reality of macro-economic reform, less government intervention, and smaller budgets meant that “the federal government has incentives to accommodate the provinces, as they have reason to co-operate with the federal government in a joint enterprise for national and regional development” (ibid., p. 190). This joint enterprise requires institutionalized FMCs.

Indeed, a key characteristic of the Canadian economy is regional development,³⁰⁹ which is interpreted as “each government being mobilized to represent the major organized interests within its borders” (Thorburn, 1985, p. 118). Such province-led development was done deliberately without Ottawa, particularly after the National Policy’s relevance was reduced during and after the Great Depression (Stevenson, 1980). The provinces erected a number of institutional buffers that cocooned resource industries from competition (Chambers & Percy, 1992, p. 46). As well, David Cameron (2012, p. 50) argues that Québec’s Quiet Revolution “broke trail for the other provinces and inadvertently encouraged them to pursue their own processes of redefinition and regional development”. The pursuit of international liberalization by Ottawa and of the regional/provincial policy orientation by provincial governments produced a contradiction that had to be confronted eventually:

The reduction of international barriers made it easier for Canadian firms to conduct business in foreign markets. For this reason, the continuing presence of interprovincial trade barriers acts to divert trade flows to where it has become less restricted. Just as lowering the water level in a river reveals jagged rocks

³⁰⁹ See Thorburn (1985) for a province-by-province break-down of economic development.

hiding at the bottom, the lowering of international barriers to trade revealed interprovincial barriers to trade (Beaulieu, Gaisford, & Higginson, 2003, p. 24).

In the long-run, the regional/provincial orientation may have contributed to Canada's reliance on the American market far above and for longer than if it had sought a more open, less fractured internal market. The fact that Canada is already highly regionalized, economically and politically, was reinforced by development activities: "Ottawa and the provinces assessed earlier federal development policies differently and represented distinctive identities and interests", which caused IGR conflict and a lack of coordination (Haddow, 2012, p. 226). Conflict continued when the 'ready-made' industrial policy of free trade as advocated by the 1985 Macdonald Commission³¹⁰ left provinces to fill the vacuum created by Ottawa's abandonment of activist industrial policies (Hall, 1998). Larry Grossman, leader of Ontario's Progressive Conservatives in the late-1980s, articulated a vision of spiraling decentralization as uncoordinated economic policies led to the disintegration of the nation. In response, he advocated for the elimination of interprovincial trade barriers through provincial policies (Grossman, 1983, p. 168). It is no coincidence that around this time the Macdonald Commission was investigating Canada's balkanized internal market yet it still took almost a decade for the AIT to come to fruition.

Over 20 years after Grant's writing, the logical conclusion to liberalize and internationalize burst onto the public stage in the 1988 'free trade election'. A poignant and lasting image from that election is a Liberal campaign TV commercial that shows the erasure of the Canada-USA

³¹⁰ The Royal Commission on the Economic Union and Development Prospects for Canada was appointed in 1982 by PM Pierre Trudeau in response to the 1981-82 recession to examine the Canadian economy and its political institutions. Chaired by Donald S. Macdonald, former federal Liberal Cabinet minister, the Commission was the largest in Canadian history and reported to PM Brian Mulroney in 1985.

border by trade negotiators. The commercial reflected the outcome of the election, in which Canadians voted for free trade yet successfully communicated that “the trade deal must not put at risk those things that set us apart as Canadians” (Carmichael, Macmillan, & York, 1989, p. 4). Yet rather than embrace Grant’s criticisms, successive governments have wholeheartedly accepted the liberal-continentalist policy despite Canada’s regionally-divided economic context. Even the Liberal Party of Canada did an about-face on free trade between the 1988 and 1993 elections.³¹¹ Grant’s warning for Canada about integration is reminiscent of Horne’s for Australia: that the current economic trajectory was insufficient and required, first, an understanding of what the issues are and, second, the will to change the trajectory. It took Canada and Australia many years to heed the warnings of writers like Horne and Grant that neither country was in fact very lucky at all.

The liberal-continentalist orientation was heavily favoured by business³¹² and was the final recommendation of the Macdonald Royal Commission, which was tasked to investigate the growing balkanization of the Canadian economy. It encouraged governments to focus on “enhanced productivity growth and a stronger competitive position” (Quoted in Leslie, 1987, p. 63) as the solution to Canada’s economic woes.

By the 1980s, it was increasingly evident that the Canadian economy was in trouble: “in or about 1980, Canada reached a high point and has been slipping, relatively speaking, since” (J. Martin, 2010, p. 340). Canada’s lagging productivity was evidenced by a large trade deficit in manufactured goods (except cars) and by a lower level of productivity growth relative to other

³¹¹ See L. Martin (2003).

³¹² See Duncan Cameron (2007) on the role of business in advocating for free trade, beginning in the mid-1970s.

industrialized economies. These problems were reflected in Canada's current account at the time, whereby the "two largest negative contributors to Canada's balance of trade are the payments associated with foreign ownership of economic assets in Canada and...the interest paid to the foreign holders of Canadian debt" (Miljan, 2012, p. 150). By the mid-1990s, interest payments on the existing federal debt of \$600 billion – one-fifth of which was owned by foreign sources – became a major catalyst for implementing austerity measures and seeking greater economic efficiency (ibid., p. 143).

The integrity of the economic union was further compounded by the fact international trade generates jobs and higher productivity whilst interprovincial trade generates only jobs; a 10% increase in each type of trade increases GDP per capita by 6.3 and 5.1% respectively, yet productivity only increases with international trade, by 4%, and practically nil for interprovincial (Coulombe, 2003).³¹³ Internal barriers to trade promote regional economies but prevent economies of scale at the national level thereby contributing to the problem of lagging overall productivity and competitiveness.

Thus, like Australia, Canada is reliant on foreign investment to propel its economy and also on foreign capital markets to fund its debt, which if left to grow unchecked could become a drag on domestic economic growth and investor confidence. Any solution required fixing the current account problem, i.e. controlling spending at all levels of government and increasing and diversifying exports *as well as* increasing domestic economic efficiency. Removing or reducing

³¹³ This is replicated by a TD Bank study, which found that international trade increased productivity for those companies by 5-12% whilst domestic market companies saw a decline between 0.4-10% (see Mandel-Campbell, 2007, p. 69).

internal trade barriers could potentially add up to one percentage point to Canadian GDP, the equivalent of about \$6-7 billion (Leeson, 2000, p. 8).

The goal of domestic reform was an important part of the policy mix because international trade is a misnomer. Helliwell (1998) found that national markets are linked by threads of foreign trade and investment. These threads were important but they also presented certain problems: Chambers and Percy (1992) concluded the Western provinces' volatile economy could potentially worsen with free trade and indicated that a more robust and efficient domestic market could help foster trade diversification, thereby reducing volatility. The point is that governments ignore the domestic economy at the peril of economic growth and prosperity, especially with the advent of USA free trade.

Mandel-Campbell (2007) recognized the problem of internal barriers when she laments Canadian corporations' inability to leverage their position in the domestic market to compete internationally. Part of the problem is our status as a 'lucky country', what Mandel-Campbell calls the 'Canada syndrome': natural wealth, small domestic market, and proximity to the USA means that Canadian corporations are skimmers, exports are 'extra gravy' (ibid. p. 52). Less colloquially, the domestic market does not prepare businesses for greater international competition, thereby placing a ceiling on growth: "Resources in Canada are viewed as a public utility whose prime purpose is to dole out jobs and insulate Canadians from the harsh realities of the marketplace" (ibid., p. 137). The insulation is not only from open international competition but also domestic due to the number of interprovincial trade barriers.³¹⁴ Mandel-Campbell also laments the lack of

³¹⁴ There is debate on whether Canada benefits more from interventionist policies, which naturally throw up barriers, or from free trade; see A. Smith and Anastakis (2014).

leadership in correcting the situation. Leaders with vision should be able to construct “a competitive Canadian economy, vigorously involved in the global economy, [that] will lead to a more prosperous Canada” (Hart, 1992, p. 117).

In its investigation of the Canadian economy, the Macdonald Commission adopted the view that international tariffs were a bigger problem than internal barriers when considering the structure of Canadian industry because the former caused “too many different products [to be] produced in too few plants at too high a cost” (Chambers & Percy, 1992, p. 75). It had evidence from the 1965 Auto Pact that free trade “rationaliz[ed] production and increas[ed] trade, while achieving and then maintaining fairly balanced total production on the two sides of the border” (Helliwell, 1998, p. 33). Correcting the distortions and reaping the benefits meant advocating for a FTA.³¹⁵ The Commission’s original concern with internal trade thus gave way to its surprise conclusion that Canada-USA free trade was the way forward (Doern & MacDonald, 1999, p. 40). A FTA was a “leap of faith”, according to the Macdonald Commission (J. H. Thompson & Randall, 2002, p. 283),³¹⁶ whilst Chapman (1996) described it as Ottawa “hedging” its bets with regard to the outcome of protracted General Agreement on Tariffs and Trade (GATT) negotiations. There was also a growing sense of urgency to avoid American protectionism by securing free trade access (W. Grant, 1989). Nevertheless, the other half of the solution to Canada’s economic woes – reforming the internal market – was left by the wayside for the time being.

³¹⁵ The Macdonald Commission also sought changes to the constitution, just like the Rowell-Sirois Commission (see Eggleston, 1946). However, whereas past HoG summits amended the constitution with regard to unemployment insurance, amendments regarding the economic union failed, necessitating a turn to IGR to achieve economic reform.

³¹⁶ The leap of faith specifically referred to the projected boost to long-term productivity, which Jackson (2007) argues never emerged.

The results of free trade were impressive. NAFTA created 3.1 million new jobs, a 125.5% increase over pre-NAFTA employment (Miljan, 2012, p. 154). Helliwell, Lee, and Messinger (2002, p. 47) conclude that “the primary role of the FTA appears to have been to increase direct trade flows between Canada and the United States” with some of the flow explained by trade diversion as imports of US goods replaced imports of interprovincial goods. Perhaps the Macdonald Commission’s recommendation was not all that shocking considering that trade with the USA was growing, as shown in the increase in manufacturing’s share of exports and in exports as a share of GNP, exports which were directed towards the USA (Wonnacott, 1987, p. 59). Canada therefore became a committed free trader with its southern neighbour. Indeed, Canada’s economy has become more reliant on exports overall, with exports comprising 25% of GDP in mid-1980s, growing to 45% by 2000 and leveling off at 30% by 2013 (World Bank, 2015b).

Canada and Australia are both lucky countries owing to their abundance of resources. Concerns emerged in both countries that their long-term survival and prosperity were threatened if they continued to rely on their semi-peripheral status. For Canada, the result could be its existence as a mere appendage of the USA whilst Australia could exist by virtue of its island continentalism but as a backwater of the world economy. Neither would control their own destiny if they could not or would not change. Grant in Canada and Horne in Australia projected these results and sought to inform their respective readers of the consequences in the hopes of changing the trajectories they foresaw. And whilst both countries made strides to address the problem, the fact that both writers are still relevant in contemporary public discourse is testament to the weight of the issues and the challenges that remain. Examining the HoG summit institutionalization process of both countries is a step toward understanding how to deal with

the great issues examined by both authors, such that both federations remain vibrant, survive on their own merits, and control their own destinies.

Reforming the Economic Union

In the 1980s and 1990s, Australia and Canada confronted the challenge of adapting to world economic shifts. Adaptation was not automatic and both countries faced protracted economic crises. This section outlines the Canadian effort at economic reform from repatriation through to the agreement to negotiate an internal trade agreement. At first, Canadian HoG sought to change the basic rules of the economic union by amending the constitution. When that effort failed, leaders had little choice but to rely on intergovernmental summits and negotiations to achieve reform.

Reforming the economic union had been on governments' agenda for some time. PM Pierre Trudeau's proposals for amending and repatriating the constitution included securing the economic union, which was "the start of a 14-year process that would lead to the AIT" (Knox, 1998, p. 141). Trudeau proposed rewriting section 121 of the *British North America Act, 1867*, which outlawed interprovincial tariffs yet over time proved a weak tool for protecting and governing the economic union.³¹⁷

The 1980 proposal sought to expand the protection of the economic union beyond tariffs to any discrimination "that unduly impedes the operation of the Canadian economic union"

³¹⁷ Since Confederation, courts have reduced the significance of the "common market clause", see Howse (1992). Section 121 of the *Constitution Act* reads as follows: "All Articles of the Growth, Produce, or Manufacture of any one of the Provinces shall, from and after the Union, be admitted free into each of the other Provinces". Some argue that the courts have interpreted Section 121 too narrowly, see Blue (2011); also see Safarian (1974) and Trebilcock (1987). On 29 April 2016, a NB judge struck down the province's limitations on cross-border beer sales as a violation of Section 121, see A. White (2015).

(quoted in Trebilcock & Behboodi, 1995, p. 24). Trudeau argued for an updated federal commerce power as well as federal paramountcy with regard to interprovincial trade in resources in return for the Western provinces' demand for full taxing authority on resources in a new section, designated 92A. A similar package deal had been proposed to the provinces during negotiations in the 1970s but federal intransigence increased remarkably, between Trudeau's re-election in 1980³¹⁸ and the Supreme Court's 'patriation' reference in 1981, to the point that Ottawa's position threatened to scuttle the package deal, and with it the entire repatriation. Saskatchewan and Alberta's own insistence eventually won the day. The provinces gained legislative control over resource development and taxation without granting Ottawa enhanced powers over the economic union; the amending formula and *Charter of Rights and Freedoms* were higher on Trudeau's list of priorities (Meekison, Romanow, & Moull, 1985).³¹⁹

After the amendment and repatriation of the Constitution, Ottawa sought other means to reform the economic union. The appointment in 1982 of the Macdonald Commission and the announcement of free trade negotiations with the USA were two key developments. As well, a review of competition policy was ordered (see D. Brown, 2002). When the Progressive Conservative Party took power, PM Brian Mulroney launched the 1984 *Agenda for Economic Renewal*, which focused on encouraging voluntary action from the provinces.³²⁰ These efforts led in 1987 to the establishment of the Committee of Ministers on Internal Trade (CMIT), which

³¹⁸ Trudeau's quick return to federal power and a resounding 'no' vote at the 1980 Québec sovereignty referendum helped to bolster his resistance to province-building.

³¹⁹ See also Trebilcock (1987), Howlett (1991), and Knox (1998).

³²⁰ PCO FOI request (A-2014-00381/JL): Doc. 1-0038-93MC(01), 18 February 1993, "Memorandum to Cabinet: Negotiations on Interprovincial Trade," p.11.

provided the internal trade issue “a lasting forum for governments, officials, and Canadians to monitor, and participate in, the internal-trade policy debate” (Doern & MacDonald, 1999, p. 43).

After Meech Lake,³²¹ Ottawa and all the provinces save Québec launched a new, broader round of constitutional negotiations that led to the Charlottetown Accord of 1992. Once again, a rewriting of section 121 was proposed to strengthen Ottawa’s powers over interprovincial trade. A new section, designated 91A, was also proposed to grant the federal Parliament a direct role in positive economic integration – harmonization and other economic policies of national scope. A new Council of the Federation – comprised of federal and provincial ministers or their representatives – was envisioned to oversee and approve Parliament’s use of the proposed section 91A powers (Trebilcock & Behboodi, 1995, p. 28). In the end, the new section was omitted from the final package and the rewritten section 121 were regarded “as a sellout of the goal of strengthening the constitutional protection of the Canadian economic union...[by including] a massive set of exceptions that threatened to overwhelm the initial prohibition on internal barriers to trade” (ibid., p. 31). Regardless, the rewritten section 121 was also omitted from the final agreement. What was included was a simple promise to look at the issue at a future FMC. Academic analysis agrees that “it was foolish to attempt to deal with [internal trade] issues through constitutional amendment; many issues do not lend themselves to easy resolution through broad constitutional principles” (ibid., p. 84). Nevertheless, as Courchene (1991, p. 46)

³²¹ Negotiated by PM Brian Mulroney and the Premiers on the lake’s shores, the Accord’s purpose was to amend the Constitution in order to secure Québec’s political consent, which it had withheld when the Constitution was last amended in 1981. The Meech Lake Accord, which was primarily concerned with Québec’s distinctiveness and enhanced provincial powers, had to be ratified by Parliament and all provincial legislatures within three years. When unanimous consent in the Manitoba Legislature was withheld by MLA Elijah Harper, and when Newfoundland Premier Clyde Wells cancelled a free vote on the agreement in the House of Assembly, the deadline came and went, nullifying the Accord.

argued, the reality of international financial liberalization “demands that Canada put its domestic house in order”.

The failure to reform the constitution after its defeat at the 1992 referendum meant that no new economic powers or economic union decision-making processes forthcoming. The implementation of the FTA during this time coupled with pressure from world economic shifts and Canada’s growing debt and faltering productivity served only to increase pressure on politicians to deal with the inefficiencies and declining competitiveness of the domestic economy. In this situation, observers noted that “it seems difficult to know whether one can talk at all about a national economy in Canada” since the different regions rely less and less on each other, which “chips away at some of the cement of confederation” (Simeon, 1991, p. 286). Post-Charlottetown referendum, it was time to focus on specifics.

The Road to the AIT

Doern and MacDonald (1999) and D. Brown (2002) argue that the AIT resulted from the convergence of several policies and events, including the declining relevance of industrial policies, the pursuit of free trade agreements, the failed constitutional negotiations, and increasing federal-provincial interdependence on economic policy. Others at the time were looking to the EU’s ‘1992 program’ of internal trade reforms as an example to Canada (see Sapir, 1991). Still others were concerned about export diversification in light of Canada’s dependence on resources and the need to support new research and investment rather than create buffers (Chambers & Percy, 1992, pp. 56, 59). The following sections explore these issues to understand how the AIT and the mechanism of continuous negotiation were launched.

As HoG grappled with the constitutional negotiations in the early 1990s, some intermittent headway was made on reducing internal trade barriers when agreement was reached on beer marketing and government procurement; “a signal was sent by the CMIT that intergovernmental negotiations were possible” (Doern & MacDonald, 1999, p. 44). The Agreement on Government Procurement eliminated discriminatory purchasing policies of provincial governments on amounts over \$25,000. The Intergovernmental Agreement on Beer Marketing Practices sought to remove restrictions on beer trade, thereby allowing “all Canadian beer products to be sold in both the Liquor Control Board of Ontario (LCBO) and Brewers Retail stores (BRI). In fact Moosehead is currently sold in the LCBO and recently became available in the BRI. Since [its introduction in] May [1992], over 610,000 cases (6/pack) have been sold in Ontario”.³²² Ontario also signed an agreement with BC and Québec to provide greater access for wine, spirits, and cider (which had to be updated at the 2016 CoF meeting in Whitehorse³²³).

The CMIT’s progress supports the notion that Ottawa and the provinces could collaboratively govern a decentralized economic union – one of the paradoxes of Canada’s ‘federal condition’. It is the opposite conclusion of Robinson (2003, p. 228), who argues that free trade agreements should lead to centralization and increased conflict between federal and provincial governments. Some of that collaboration was also occurring bilaterally. In 1993, several letters describing the automotive sector’s competitive position vis-à-vis the USA were sent by Ontario’s New Democratic Party (NDP) Premier Bob Rae to both Progressive Conservative

³²² Totalling approximately \$6 million in sales. Archives of Ontario, Folder B501234 – CMIT March 18/93, “Minister’s Briefing Note: Follow-up on Existing Agreements, Beer Marketing Practices Issue,” 18 March 1993, p.1.

³²³ See McGregor (2016).

and Liberal Prime Ministers in Ottawa.³²⁴ No matter who was in power, both federal political parties needed to address the US-Canada bilateral relationship, particularly foreign competitors “appeas[ing] American trade sentiments by investing directly in the US as opposed to coming to [Ontario]. We need a common political response to this perception”.³²⁵ As soon as Liberal leader Jean Chrétien became Prime Minister in 1993, Rae asked for a meeting of Ottawa and Ontario industry ministries to investigate joining a USA R&D initiative on fuel.³²⁶ These were bilateral regional economic issues between the two governments; neither FMCs nor internal trade were a factor in Ontario’s competition with the USA.

Ontario’s bilateral dealings with Ottawa and the CMIT’s limited progress indicate that as trade policy increasingly touched upon provincial jurisdictions, provincial governments were unwilling to relinquish power to cooperative institutions in order to compensate a loss of policy manoeuvrability from free trade:

there remained a pervading concern by provincial governments that to remove barriers to domestic trade and to eliminate or harmonize other measures that make the economic union less efficient would reduce their economic jurisdiction and limit their policy and legislative flexibility and authority in other areas” (Knox, 1998, p. 141).

It was a zero-sum game, and Canada’s intra- and inter-state federal structures – more precisely the lack of the former and the latter’s minimalist institutionalization – were not up to the task of managing policy coordination simultaneously across multiple policy areas.

³²⁴ See also Gilpin (1972, p. 139), who states that leadership is required to deal with exposure to international pressure. For example, he compares Japanese centralization with EEC decentralization.

³²⁵ Archives of Ontario, Folder B368296 – Correspondence with Brian Mulroney, “Letter from Rae to Mulroney,” 4 March 1993, p.3.

³²⁶ Archives of Ontario, Folder B368296 – Correspondence with Jean Chrétien, “Letter from Rae to Chrétien,” 29 November 1993, p.2

Once again, we are presented with the Canadian contradiction of economic liberalization and internationalization via weakly institutionalized FMCs and, in the case of internal trade, a weakly institutionalized ministerial council. While there was progress on smaller issues, larger questions of economic policy – particularly concerning positive economic integration³²⁷ – succumbed to the notion that “the degree of... intergovernmental conflict is...conditioned by the political distance between peripheral aspirations and the central process of decision making” (Hueglin, 1990, p. 12). In short, it was extremely difficult for HoG to make collective political decisions. Federalism itself was not the problem, since the above discussion points to concrete examples of cooperation; and there are additional examples of cooperation from this time, such as provincial involvement in international trade negotiations and Team Canada missions (Simeon, 1991, p. 291). The problem was how the federation, particularly its IGR system, was organized.

Inwood et al. (2011, p. 416) conclude that “in most policy areas it is no longer a question of exclusive jurisdiction..., but a question of how jurisdiction, responsibility, accountability, policy purposes, and public resources are shared”; what they refer to as intergovernmental policy capacity,³²⁸ a concept that emerges directly from Canada’s ‘federal condition’. Yet Inwood et al. find that officials involved in IGR are focused internally and “showed little interest in the Constitution, courts, Parliament, political parties, international influences, the public, and the role of ideas” (ibid., p.459). Political leaders are the prime agenda-setters within the IGR system; what HoG are focused on is what the system is focused on, causing officials to become frustrated with the lack of opportunity to deal with complex issues (ibid., pp. 462, 465). There is a sense

³²⁷ See Purvis and Raynauld (1993, p. 133).

³²⁸ See also the concept of administrative capacity (Milio, 2010).

that intergovernmental agreements are unable to change long-established and deeply engrained modes of behaviour. HoG are uninterested in IGR, turf wars amongst officials are common, line departments resent central agencies, and informal relations and trust ties are seen as more important than formal ties. Leadership is clearly missing, but “like the weather, everyone talks about [leadership], but no one does anything about it” (Inwood et al., 2011, p. 419).

Bureaucrats were not the only ones signalling their frustration. According to Doern and MacDonald (1999), pressure to deal with internal barriers also came from business lobbies.³²⁹ The business community argued that it was preposterous that there existed more barriers to internal trade than to international trade (see Knox, 1998). Consultations with several associations revealed complaints regarding Ontario and Québec as “2 major culprits,” with the Ontario Chamber of Commerce indicating that Québec is “a major ‘instigator of interprovincial trade barriers’”. Most associations were concerned about local procurement policies, labour mobility, and transportation.³³⁰ Examples include “restrictions placed on workers/companies who want to work or do business in Quebec”, the fact that “Ontario’s open bidding practices are losing the province money and jobs while other provinces (especially Quebec) maintain protectionist policies”, and the “different professional licensing regulations between provinces”.³³¹ According to Courchene and Telmer (1998), these disagreements could do great harm to the federation as a whole, especially since the larger provinces were already relying more on international trade, once the dessert of Canadian trade, rather than the traditional meat and

³²⁹ Although it has been noted how difficult it is to marry IGR and non-governmental participants, see J. Simmons (2008, p. 371).

³³⁰ Archives of Ontario, Folder B501234 – CMIT March 18/93, “Interprovincial Trade Barrier Consultations,” p.1.

³³¹ Archives of Ontario, Folder B705175 – Consultations with Private Sector, “Summary of the Companies, Associations and Municipalities to be Contacted, re Interprovincial Trade Barriers,” 18 June 1993, p.2.

potatoes that was internal trade. If Canada's existence is inextricably linked to east-west trade, then these disputes were cause for concern.

The Board of Trade of Metropolitan Toronto wrote to the CMIT that even though procurement and alcohol were barriers that the CMIT was currently dealing with, "the real problems faced by the private sector in Canada are infinitely broader...even the term, 'interprovincial trade barriers', is far too limiting in our view". It noted such issues as "excessive regulation of commercial activity," the increased costs due to provincial monopolies, and federal policies that distort the market, such as regional standards for employment insurance and un-harmonized sales taxes.³³² The Canadian Manufacturers' Association (CMA) was perhaps more blunt: "Canada's productivity is being undermined by hundreds of interprovincial barriers to trade in goods and services affecting an estimated 10-15% of GDP [approximately \$6 billion per year]".³³³ It stated that governments know about the problem, are moving too slowly to fix it, and should, like the EU, adopt an action plan for reform.³³⁴ Although the Canadian economy was slowly liberalizing, governments still took a protectionist stance with their economic and regional development policies. The incongruence between internal protections and internationalization was one of the reasons why the economic union was placed at the top of the IGR agenda after

³³² Archives of Ontario, Folder B705175 – Communications: Canada, "Letter from Toronto Board of Trade to CMIT Co-Chairs," 25 November 1993, p.1. Similar views were also expressed by the Insurance Bureau of Canada.

³³³ Library of Canada, Ottawa (herein Ottawa), HF3226.5 R88 1991, "Canada 1993: A plan for the creation of a single economic market in Canada," April 1991, p.1. This figure has been heavily criticized, see Copeland (1998), who came up with a figure of 0.1% of GDP rather than 1%.

³³⁴ In Europe, this is referred to as the '1992 single market program', see Cecchini, Catinat, and Jacquemin (1988); Ross (1995). For more comparisons between Canada and the EU, see Crowley (2004); Demers and Demers (1995); Leslie (1996).

the Charlottetown referendum (an incongruence the CMA believed was “a disturbing statement about our political union”³³⁵).

Both Canada and Australia faced a massive restructuring of their respective domestic economies during this period. The major difference between the two cases is the external economic context that surrounded the internal trade issue. In Australia, the perception of economic crisis was compounded by the ‘turn to Asia’. Together these issues generated a sense of urgency amongst HoG to engage a cooperative process of reform; the risk of not reforming was simply too great. In Canada, the perception of economic crisis confronted the economy’s reliance on USA trade. With the FTA completed, Canada had reduced its risk; even though there existed an acknowledgement of the domestic economy’s weaknesses, securing Canada’s access to the market of its most important trading partner removed much of the urgency to reform.

Deciding on the AIT’s Mandate

The road to the AIT was indeed bumpy. Internal trade reform had to wait and hope for promised constitutional changes, compete with free trade negotiations, and be content with initially achieving only a couple of minor changes to procurement and alcohol restrictions. Once the constitution and FTA were off the agenda, reforming the domestic economy took centre stage. All that was needed now was to convince the provinces to buy into and launch a reform process.

The Mulroney government’s 1991 throne speech stipulated its ‘Canada 1995’ target “to see barriers to interprovincial trade and investment come down by 1995 so that Canada becomes

³³⁵ Ottawa, HF3226.5 R88 1991, “Canada 1993: A plan for the creation of a single economic market in Canada,” April 1991, p.2.

a single, integrated market” (Government of Canada, 1991).³³⁶ The target emanated from the government’s 1984 *Agenda for Economic Renewal*, which “identified barriers to interprovincial trade and impediments to the efficient operation of the internal market”.³³⁷ At that time, Mulroney sought to increase Canada’s competitiveness by establishing Industry, Science and Technology Canada (ISTC), which separated regional development from competitiveness policies. The CMIT was established to coordinate federal-provincial efforts at improving competitiveness.

By the early 1990s, these pledges to reform became part of *Inventing Our Future: An Action Plan for Canada’s Prosperity*, released in October 1992 by Industry Canada. According to an Ontario government briefing, the report sought “the promotion of innovation” in areas of industrial policy (trade, technology, and regional development), continuous learning, and an inclusive, equitable society. The industrial policy aspect specifically highlighted the elimination of interprovincial trade barriers as well as fiscal coordination, tax harmonization, deficit reduction, coordination of federal and provincial technology support and trade development programs, and the development of a worker adjustment program.³³⁸ Ottawa and the provinces were abandoning the pursuit of national economic development – hastened in part by growing deficits – and were gravitating towards more network-based, innovation-supporting policies in which federal-provincial cooperation is on a case-by-case basis (Haddow, 2012, p. 232).

³³⁶ No mention is made in the throne speech about the CMA’s call for a ‘1993 program’ even though the throne speech on 13 May 1991 occurred one month after the CMA paper was released. Likewise, the CMA paper does not reference the 1984 *Agenda for Economic Renewal*.

³³⁷ PCO FOI request (A-2014-00381/JL): Doc. 1-0038-93MC(01), 18 February 1993, “Memorandum to Cabinet: Negotiations on Interprovincial Trade,” p.11. At that same time, Premiers from Ontario and BC were calling for reducing internal barriers to trade (see Ottawa, HF1479 M35 1985, “The Canadian Common Market: Interprovincial Trade and International Competitiveness,” October 1985, p.1).

³³⁸ Archives of Ontario, Folder B501234 – CMIT March 18/93, “Briefing Note: Federal Prosperity Action Plan”, 17 November 1992, p.1.

It is important to note that, for a moment, the issues of fiscal federalism – in the form of coordinated tax policies – and internal trade were linked together as critical to the promotion of economic prosperity. Ontario's analysis was that the federal plan "takes governments to task for our declining competitive position, but only encourages the private sector to 'do better'. Provincial governments' ability to act effectively in the economic development field will be restricted if the *Action Plan*'s recommendations on harmonization of federal and provincial fiscal policies are implemented".³³⁹ Ontario Economic Development Minister Frances Lankin³⁴⁰ was quoted as saying that "Ontario already has serious grievances with Ottawa over our fair share of federal money...Ontario will need a new financial arrangement with Ottawa...one that's more transparent and doesn't include hidden deals between Ottawa and other provinces".³⁴¹ Rather than focus on the coordination of fiscal policies, the provinces were looking to examine fiscal federalism in the form of intergovernmental transfers, precisely the same issue Hawke used to entice the states to join his 'closer partnership'.

Mulroney's *Action Plan* required the involvement and cooperation of the provinces, which his government sought via a HoG summit. At their 1991 Annual Conference, Premiers had already noted "the urgent need for First Ministers to resume meeting annually to discuss critical economic problems" as well as the stability of federal transfers. They wanted "a national

³³⁹ Ibid., p.3.

³⁴⁰ Lankin was described as ambitious when she was moved from Health to Industry: "[Premier] Rae...felt they needed someone to repair strained relations with business and transform the moribund Ontario Industry ministry into a vehicle for economic renewal. Who better than the government's most competent minister?" (Walkom, 1994, p. 67).

³⁴¹ Archives of Ontario, Folder B705175 – Communications: Ontario, "Rae devises plan on Quebec," *Toronto Star*, 27 May 1994, p.1.

industrial and economic strategy”.³⁴² To that end and despite the ongoing constitutional negotiations, Mulroney convened a ‘FMC on the Economy’ in December 1991 and February 1992, which led to the release of a formal communiqué at the conclusion of the March 1992 FMC.³⁴³ Yet before the conferences were held, some Premiers voiced specific reservations. Alberta Premier Don Getty wanted “to know the agenda and I want to see it as a constructive meeting that will work on solutions, that will be pulling our country together, that will be building the economy...But I don’t think our nation would be well served if we had something that was not constructive but rather was a process of tearing things down”. When asked if Québec’s attendance was “essential”, he responded that “I don’t see it as absolutely essential but for the best possible results it would be better”.³⁴⁴ With HoG discussing microeconomic reforms, the mechanism of continuous negotiation was poised to engage.

At the March 1992 FMC, HoG committed themselves to the ‘Canada 1995’ target by vowing to construct a new set of rules for removing and preventing internal trade barriers. Their goal was to refashion the domestic market to be as open and accessible as the international marketplace. To that end, they instructed the CMIT to “accelerate” its work program under a deadline of 31 March 1995³⁴⁵ and issued a mandate for the “elimination of discriminatory practices and impediments to trade”.³⁴⁶ No evidence was found to suggest that HoG considered

³⁴² Archives of Ontario, Folder B368449 – Annual Premier’s Conference August 1991, “Final Communiqué,” 26-27 August 1991, p.1-2.

³⁴³ Québec Premier Robert Bourassa attended the December 1991 meeting but his finance minister attended the other two (Canadian Intergovernmental Conference Secretariat, 2004).

³⁴⁴ Québec Archives, Box 24 A 001 08-05-006B-01, Folder 2005-10-003\274, “Premier Getty & PM Mulroney News Conference,” 5 December 1991, p.3.

³⁴⁵ Bibliothèque et Archives nationales du Québec (herein BAnQ) Montreal, CE32-X51 1992 cof, “First Ministers’ Meeting on the Economy,” 24-25 March 1992 (Doc 800-030/017).

³⁴⁶ Archives of Ontario, Folder B501234 – Meeting: Chief Negotiators-Task Force of Officials on Internal Trade, “Note to Task Force of Officials Re the CMIT and Constitutional Change,” 22 September 1992, p.1.

undertaking these reforms themselves. Rather, “it is assumed that the CMIT should provide advice to First Ministers on the Canadian common market”.³⁴⁷ As well, no mention was made of resuming yearly FMCs. Given that such meetings would be established as part of the Charlottetown Accord, it is safe to assume that HoG believed they would at least monitor the file at their next meeting.

In a sharp reversal from its previous attempts at economic union reform, Ottawa put its own policies on the table and would not seek special federal control over implementation: “Federally created barriers to trade would be covered as fully as provincially created ones” (D. Brown, 2002, p. 153). The provincial and federal governments also committed themselves to “cooperatively promote” exports, which would exist alongside an already extensive base of cooperation in the area of international trade. The provinces especially were supportive of Ottawa taking an “assertive” approach to defending Canada’s trading rights in international agreements.³⁴⁸ Yet behind the scenes, provinces were arguing with each other. According to BC Premier Mike Harcourt, “Quebec lumber interests threatened to sever the countervail agreement with the US. It was so outrageous and potentially damaging a position to BC’s lumber interests that I, in turn, threatened to boycott the constitutional table” (Harcourt & Skene, 1996, p. 80). Certainly bad omens for a renewed reform effort.

By May 1992, the CMIT drafted three principles to enhance internal trade and announced a moratorium on the creation of new barriers.³⁴⁹ The three principles were “that governments

³⁴⁷ Ibid.

³⁴⁸ Ibid.

³⁴⁹ Archives of Ontario, Folder B501234 – Meeting: Chief Negotiators-Task Force of Officials on Internal Trade, “Press Release: Internal Trade Ministers Meet,” 1 May 1992, p.1.

should: 1) 'treat people, goods, services and capital equally irrespective of where they originate in Canada'; 2) 'reconcile standards and regulations...'; and 3) 'ensure that their administrative policies operate to provide for the free movement of people, goods, services and capital'".³⁵⁰ In the application of these principles, all governments agreed to "full disclosure...; exceptions and transition periods as well as special needs consistent with regional development objectives in Canada; and supporting administrative compliance mechanisms".³⁵¹ The CMIT co-chairs – the Federal Minister of Industry and MB Minister of Industry Eric Stefanson – wrote to Ontario that it expected all governments to begin reviewing "legislation, regulations, policies and practices to identify those which do not adhere to these open market principles" (the co-chairs also expected "that we participate fully in intergovernmental efforts"). As well, the CMIT wanted "to address destructive competition for investment and enhancing trade and investment linkages as well as larger competitiveness issues".³⁵²

The defeat of the Charlottetown Accord at the October 1992 referendum seemed to have little impact on the CMIT. In the lead up to the December 1992 CMIT meeting, deputy ministers noted that the agenda was "very ambitious" and recommended that Ministers deal with "the broader issues which underlie this process, e.g., linking economic development responsibilities with the process of reducing interprovincial trade barriers". The broader discussion was necessary because many issues were still in the research phase.³⁵³

³⁵⁰ PCO FOI request (A-2014-00381/JL): Doc. 1-0038-93MC(01), 18 February 1993, "Memorandum to Cabinet: Negotiations on Interprovincial Trade," p.11.

³⁵¹ Archives of Ontario, Folder B501234 – Meeting: Chief Negotiators-Task Force of Officials on Internal Trade, "Press Release: Internal Trade Ministers Meet," 1 May 1992, p.4.

³⁵² Archives of Ontario, Folder B501234 – Meeting: Chief Negotiators-Task Force of Officials on Internal Trade, "Letter from CMIT Co-Chairs to ON Minister of Industry Ed Philip," 29 June 1992, p.2.

³⁵³ Archives of Ontario, Folder B501234 – Meeting: Chief Negotiators-Task Force of Officials on Internal Trade, "Notes for the November 24 conference call of Deputy Ministers Responsible for Internal Trade," 16 Nov 1992, p.1.

At the December 1992 CMIT meeting,

Ministers agreed to use the CMIT forum to address economic development coordination issues..., decided to establish working groups to share sector information..., agreed to share information on how they assess the competitiveness impacts of proposed legislation and regulations..., decided to continue to cooperate on initiatives to improve business access to...government services..., [and] agreed...[to] resolve many of the issues arising from counterproductive intergovernmental competition for investment. In recognition of the 'north-south' aspects of this issue, Investment Canada officials are to include...a discussion on how governments can cooperate more effectively to offset efforts by the United States to divert business investment from Canada.³⁵⁴

Clearly, regional development and Canada-USA trade were considered important elements of the internal trade reform effort, a fact which Rae's letter regarding the automotive industry did not recognize. Liberalizing the domestic economy encompassed a myriad of policies. Indeed, the CMIT noted that past efforts had only "scratched the surface of the problem in [each] particular area" and therefore Internal Trade Ministers were asked to return to their respective capitals to acquire "a clear commitment to negotiate a comprehensive agreement on internal trade".³⁵⁵ This was required because "the CMIT process is moving too far ahead of the First Ministers and where the CMIT is getting involved in constitutional issues which go well beyond interprovincial trade," specifically the issues of compliance.³⁵⁶ Thus, as in Australia, the beginning of the reform process was broadly-based and began to draw in all orders of government into a concerted and cooperative effort that signals the emergence of the mechanism of continuous negotiation.

³⁵⁴ Archives of Ontario, Folder B501234 – CMIT March 18/93, "Undertakings of the CMIT," 4 December 1992, p.1.

³⁵⁵ PCO FOI request (A-2014-00381/JL): Doc. 1-0038-93MC(01), 18 February 1993, "Memorandum to Cabinet: Negotiations on Interprovincial Trade," p.13.

³⁵⁶ Archives of Ontario, Folder B501234 – Meeting: Chief Negotiators-Task Force of Officials on Internal Trade, "Notes for the November 24 conference call of Deputy Ministers Responsible for Internal Trade," 16 Nov 1992, p.1.

However, the reform effort also attracted criticism that would eventually limit its impact on the institutionalization of FMCs. Ontario's Economic Development Ministry recommended to Premier Rae that "we should attempt to exclude from the discussion, actions designed to harmonize regulations and standards among the provinces" and it speculated that Ottawa could use the interprovincial trade agenda "to limit provincial policy capacity...[It] may also be attempting to limit the ability of the provinces to provide financial assistance to firms for economic development purposes".³⁵⁷ From the start, one of the major players was refuting the fundamental reason for engaging in microeconomic reform.

Some provinces were also pressing Ottawa on "some elaboration of the process and procedural aspects associated with the kind of negotiation". Federal negotiators noted that "flexibility is key to the process" and that "any structures established, procedures followed or ground rules adopted in the course of the negotiations are those which: the negotiators themselves see as necessary or useful, and assist in getting on with the job in agreed time frames".³⁵⁸ Ontario made clear that provincial Ministers would need to be contacted "as specific issues become more defined" in order to modify negotiators' initial mandate, to keep the provincial Cabinet informed and ask it to approve mandate changes, and finally, to decide whether to accept a final deal.³⁵⁹ There was no mention made of First Ministers' direct involvement. The onus to complete the negotiations, despite early worries about overstepping their mandate and the constitutionality of the issues, rested with Ministers responsible for

³⁵⁷ Archives of Ontario, Folder B399127 – Economic Development and Trade, "Memorandum to Rae from Industry Minister Ed Philip re Meeting of Ministers Responsible for Internal Trade," 16 December 1992, p.3.

³⁵⁸ Archives of Ontario, Folder B501234 – Meeting: Chief Negotiators-Task Force of Officials on Internal Trade, "Canadian Internal Trade Negotiations: Aspects of the Negotiating Process," 5 January 1993, p.1. This followed specific discussions between federal and provincial trade negotiators, which are detailed in the next chapter.

³⁵⁹ Ibid., p.2.

internal trade, who stated that they “intend to be involved throughout the process and monitor progress of negotiations very closely” given the “tough deadline”.³⁶⁰ The lack of direct HoG involvement as the CMIT’s mandate began to shift contrasts starkly with the moving mandate of the Australian negotiations, which directly involved the HoG. The lack of engagement by HoG evidenced here would become a larger problem.

Bob Knox,³⁶¹ senior federal negotiator and Executive Director of the Internal Trade Secretariat (ITS), attempted to address the lack of engagement when he wrote to the SK Trade Policy Branch. He recalled that officials had reached a final agreement at the December 1992 CMIT meeting on the list of sectors and issues that would constitute the negotiations and therefore noted that further amendments were no longer possible. He also stated that “extensive work has already been completed on the nature of internal trade barriers and opportunities [and that] any further research should be carried within the context of sectoral negotiations”. It was now time for Saskatchewan to “develop its own position with regard to the proposed sectors...[The] comprehensive negotiations should provide a coherent, flexible process to dismantle barriers. The comprehensive nature of discussions will in fact provide greater assurance of a balanced and regionally sensitive agreement”.³⁶² At least, that was the hope.

Ottawa wanted a comprehensive, rules-based agreement that would have broad applicability across policy sectors, which “would be applied to every government activity which

³⁶⁰ Archives of Ontario, Folder B501234 – Meeting: Chief Negotiators-Task Force of Officials on Internal Trade, “CMIT Meeting: Summary of Discussions and Decisions of Ministers,” 18 March 1993, p.1.

³⁶¹ Robert Knox passed away on 5 June 2015. He is remembered as “a champion of economic freedom in Canada”. See Macdonald-Laurier Institute, “Remembering Robert Knox,” 5 June 2015”. Retrieved from: <http://www.macdonaldlaurier.ca/remembering-robert-knox-a-champion-of-economic-freedom-in-canada/>.

³⁶² Archives of Ontario, Folder B501234 – CMIT March 18/93, “Letter from Knox to Cam Pelzer,” 6 Jan 1993, p.1.

might have an impact on internal trade”.³⁶³ Federal negotiators noted that this kind of agreement would be easier and faster to negotiate. The problem was that broad rules would require a series of dispute settlements to understand just exactly what is in the agreement, which would focus on each sector’s exemptions and therefore could limit provincial sovereignty.

The alternative was to negotiate a sector-based agreement, which would actually be comprised of a series of sector agreements bundled together under general principles that would act as a guide for each sector’s negotiations. This type of agreement would focus on specific barriers rather than a code of conduct for every government activity relating to internal trade. The advantages to this approach were clarity in negotiations, less interpretation afterwards, and a reduced focus on exemptions. The disadvantage was that a time-consuming and complex process could lack symmetry and future applicability.³⁶⁴ Alberta provided the example of window production: “A window, as a manufactured good, is currently considered to be outside the scope of the Natural resources Processing Chapter...Without a general coverage clause, internal trade in windows would not be covered unless a specific reference to windows can be found in the Agreement”.³⁶⁵ Governments could then favour locally-produced windows over other Canadian-produced windows because it is not specifically covered. In other words, a sector-based agreement would allow the provinces to retain full use of their economic powers.

With all parties at least agreed that the CMIT should begin preparing for future negotiations, Federal Industry Minister Michael Wilson submitted a memorandum to Cabinet on

³⁶³ Archives of Ontario, Folder B501234 – Text-Draft Framework Agreement & Descriptive Companion-Oct-Nov/93, “Letter from BC Chief Negotiator Robert Food to all Chief Negotiators,” 18 January 1994, p.1.

³⁶⁴ Ibid., p.3.

³⁶⁵ Alberta FOI request (2015-G-0007): Applicant Package Part 1, “Fax from Internal Trade Secretariat to Alberta: Goods,” 27 April 1994, p.441.

18 February 1993. Its purpose was to formally approve a process of internal trade reform, which was decided with the provinces at the 1992 'FMC on the Economy.' Cabinet was asked to decide "whether and how to engage the provinces in a comprehensive, multi-sector, negotiation to establish a more open and efficient domestic market".³⁶⁶ The goals of the negotiation were to establish basic rules and principles for how the interprovincial movement of goods, capital, people and services were to be handled by both orders of government, to define the application of mutual recognition, and to ensure compliance and dispute settlement. Ottawa's first priority was to have the provinces agree on "clear, concise rules-based framework for the internal market [and on] disciplines on the exercise of their sovereignty". During this process, all governments "will be negotiating the fundamental obligations, rules and disciplines which will govern their conduct in the future".³⁶⁷ This last statement contains the seed for future reforms to the IGR system. For now, the issue was limited to decision-making regarding the internal market only.

The framework for the basic rules that the federal government wanted were also established in Wilson's memorandum. These rules mirror the CMIT's three principles of internal trade, which were agreed to back in May 1992. The first rule sought equal competitive opportunities, which meant no discrimination against any out-of-province products or workers.³⁶⁸ The second rule banned reinstitution of local preferences by other measures that would decrease access to a provincial market. Third, if a rule affected access, then it must be

³⁶⁶ PCO FOI request (A-2014-00381/JL): Doc. 1-0038-93MC(01), 18 February 1993, "Memorandum to Cabinet: Negotiations on Interprovincial Trade," p.3.

³⁶⁷ Ibid., p.17.

³⁶⁸ The memorandum noted that this was equivalent to the GATT National Treatment principle.

clearly and comprehensibly communicated to any interested party. Finally, the federal government sought harmonization, and failing that, mutual recognition.

The memorandum cautioned that if BC, Ontario, or Québec refused to sign onto the negotiations, the government would not commit itself to the process. Yet it also noted “strong” support from national business associations as well as the general public’s knowledge of and support for an open domestic economy. The public and industry associations were cautiously optimistic about the initiative because of governments’ lack of progress thus far.³⁶⁹ If political capital was going to be spent so close to an election in order “to show that the federal government is acting to make the economy more efficient and able to take full advantage of the recovery to provide the kind of economic growth expected by the public”,³⁷⁰ then the negotiations had better succeed.

Ottawa would secure the provinces’ agreement to start talks by formulating a negotiating process that recognized their jurisdictional sensitivities. Rather than target provincial powers directly, Wilson hoped a comprehensive, multi-sector negotiation process was better suited to achieving reform. Wilson highlighted that past reform efforts stalled because of the perceived “limitations on the exercise of sovereign power or winner/loser comparisons”. At the CMIT in December 1992, Wilson recommended a “comprehensive multi-sector negotiation on the internal market” in the hopes that provincial governments would continuously negotiate “on the basis of the final overall balance of benefits...[since] the purpose is not to change sovereign

³⁶⁹ PCO FOI request (A-2014-00381/JL): Doc. 1-0038-93MC(01), 18 February 1993, “Memorandum to Cabinet: Negotiations on Interprovincial Trade,” p.9.

³⁷⁰ Ibid., p.15.

powers but rather how they are used”.³⁷¹ The AIT was to be a different form of IGR, a cooperative effort between jurisdictions rather than a competitive one to achieve real and tangible reforms. The Cabinet committee on Economic and Trade Policy formally authorized Wilson’s plan on 23 February 1993.³⁷² The next day, Mulroney announced he was resigning as leader of the Progressive Conservative Party. The remaining Cabinet supported the plan on 11 March.³⁷³

With federal Cabinet approval in hand, the next objective was “to reach an agreement with Provincial Governments and announce...that negotiations will begin by June, 1993 to reach a comprehensive internal trade agreement within the next two years”.³⁷⁴ The problem, as federal negotiators made clear, was that some provincial governments may “propose conditions, exceptions or limitations...[which] means that A COMPREHENSIVE NEGOTIATING PROCESS IS UNACCEPTABLE”.³⁷⁵ Anything short of comprehensive “will not be viable or credible”.³⁷⁶ The next CMIT meeting in March 1993 should seal the deal on the comprehensiveness issue.

Wilson’s notes for the March meeting recommended that, in order to reach agreement on comprehensiveness,

“you will wish to

1) Take the high road by emphasizing that:

- An open and efficient internal market is essential for the competitiveness of Canadian business, to ensure continued investment in Canada and that all Canadians are treated fairly within their own market.
- Canada must operate as a national market to gain the benefits of a national economy.

³⁷¹ Ibid., p.5.

³⁷² PCO FOI request (A-2014-00381/JL): Doc. 1-0038-93CR(01), “Report of Cabinet Committee Decision,” 26 February 1993.

³⁷³ PCO FOI request (A-2014-00381/JL): Doc. 1-0038-93RD(01)(C), “Record of Cabinet Decision,” 15 March 1993.

³⁷⁴ Archives of Ontario, Folder B501234 – Meeting: Chief Negotiators-Task Force of Officials on Internal Trade, “ISTC: Objectives and Scenario notes,” March 1993, p.1.

³⁷⁵ Ibid., p.2. Emphasis in original.

³⁷⁶ Ibid., p.1.

- Canadian Governments need to work together and provide a stable, transparent economic environment that minimizes the problems for business....
- 2) Make it a national, non-political issue.
- Provinces have been publically committed to dealing with internal trade issues starting in 1986. It is now time to get to [sic] accomplish something tangible...
- 3) Postpone confrontation.
- Everything is on the table ('no cherry picking') and 'nothing is agreed until everything is agreed' and we should want a 'clean launch' to ensure that all issues are carefully considered (no qualifications or exceptions).
 - Not all issues need to be resolved at once and some issues can be postponed but there needs to be a plan for when and how they should be resolved or when they will be reviewed
- 4) Assume Success.
- First Ministers requested the [CMIT] to resolve internal trade issues by 1995. This direction is still in place.
 - Ministers agreed [in December] to recommend a comprehensive negotiation".³⁷⁷

Wilson's strategy to garner the approval of the provinces to start negotiations on a comprehensive deal that would change the exercise of their economic powers has strikingly similar parallels to the Australian case. Industry Minister Wilson's appeal for an open and efficient internal market for the sake of competitiveness mirrors PM Bob Hawke's reasons for asking the states for a 'closer partnership'. Wilson's memorandum sought to solidify Ottawa's commitment to the process by acknowledging the need to postpone confrontation and that all parties needed to work together. Hawke too indicated that Canberra was looking to reset an often fraught relationship. In Canada, as in Australia, now was the time to reform the economy together. With Ottawa's position outlined and approved, would the provinces agree to begin negotiations?

³⁷⁷ Ibid., p.3-4.

Provincial Opposition

Ottawa's desire to liberalize internal trade on the basis of a comprehensive multi-sector negotiation now needed to be sold to the provinces. Even though reforming the economy had been on the agenda for some time and Canada faced several pressing economic challenges, some provinces still needed convincing that Ottawa's strategy was the correct one. Wilson and his successors would find that provinces had other concerns, namely, fiscal federalism, regional development, and their own economic development plans.

Wilson was provided with notes for a possible telephone conversation with Ontario Industry Minister Lankin before the March 1993 CMIT meeting. Wilson was advised to register the point that

domestic trade is as important for Ontario as international trade..., [that] there are a number of access problems for Ontario in Quebec's market and the best way to get at these is a comprehensive internal trade negotiations [especially since] the comprehensive negotiations would be one way to begin the process without immediately having to deal with an issue that is difficult for both provinces.³⁷⁸

Lankin was prepared with her own file. In it, the accusation that Ontario did not support removing barriers was debunked by highlighting its signing of the CMIT's procurement agreement and beer marketing practices agreement.³⁷⁹ Yet both of these agreements were now several years old, with little progress thereafter. Ontario's Trade Policy Branch informed Lankin that "the list of subjects to be covered by the proposed negotiation is too broad and ranges well beyond trade interests; limits need to be placed around these negotiations". It also cautioned

³⁷⁸ Ontario and Québec were locked in a dispute over access to their wine markets (Archives of Ontario, Folder B501234 – CMIT March 18/93, "Telephone discussion on Internal Trade with ON Minister Francis Lankin," March 1993, p.1).

³⁷⁹ Archives of Ontario, Folder B501234 – CMIT March 18/93, "Minister's Briefing Note on Interprovincial Trade: Allegations against Ontario," 18 March 1993, p.1

that there was a difference between a barrier that required a firm to be 'in-province', and a regulation that merely treats firms differently: "[these] may add to the paper burden imposed on business but are not trade barriers per se". It was even recognized in the Charlottetown Agreement "that these types of measures do not constitute barriers to interprovincial trade".³⁸⁰

Then, in her speaking notes for the March 1993 CMIT meeting, Lankin outlined that Ontario would support the removal of barriers, subject to certain principles. The first was that Ontario felt that its businesses "face barriers to doing business in other provinces...Ontario feels that the existing generous access we provide to our market is a minimum condition which other provinces must meet before we consider further improvements in access".³⁸¹ Thus, Ontario was not stalling the negotiations; rather it was further ahead of the other provinces and was merely waiting for the rest to catch up. Second, it noted that "differences in provincial and federal standards and regulations do not necessarily create interprovincial trade barriers". In other words, provincial sovereignty must be respected. Third, it was important that the CMIT recognize the work already completed and underway in the labour, transportation, financial, and agricultural portfolios. Fourth, "there is no need for expensive secretariats, new bureaucracies or internal trade commissions...Most disputes can be resolved through consultation between governments [at the ministerial level]. If a more formal mechanism is necessary, it must be simple and accessible, because the overall goal is to help business...[and] that our real job is help [sic] create jobs for people".³⁸²

³⁸⁰ Archives of Ontario, Folder B501234 – CMIT March 18/93, "Ministers' Briefing notes on Comprehensive Negotiating Process: Mandate and Conditions," 18 March 1993, p.1. The notes also contain lengthy explanations of Ontario's policy concerning beer, in particular addressing concerns from NB and its flagship beer, Moosehead.

³⁸¹ Archives of Ontario, Folder B501234 – CMIT March 18/93, "Introductory Remarks, CMIT, Minister's Speaking Points," 18 March 1993, p.1.

³⁸² Ibid., p.5.

Given the academic literature on Canada's federal condition, achieving Ontario's goals would seem to necessitate the institutionalization of IGR, or at the very least more intergovernmental cooperation, to deal with internal trade barriers and standards harmonization all in the name of competitiveness and liberalization. Why then does Ontario specifically rule out institutionalization as an option?

The answer lies in Ontario's priorities. In response to Ottawa's *Action Plan*, Ontario focused on its own competitiveness:

Intensifying international competition, the development and application of new technologies...are forcing us to change the way we operate...In Ontario we are focusing on...six competitive fundamentals: continuous innovation, upgrading skills, increasing technological capacity, establishing home-base activities..., developing linkages and networks and building international capabilities.

Ontario pointed to an 11.1% real increase in its R&D spending between 1986 and 1991, compared to a federal increase of just 0.5%.³⁸³ Then, in Lankin's speech at the March CMIT meeting she stated that the provincial agenda differed from Ottawa's since Ontario "stresses the need for governments to play an active role in the creation of competitive advantage...Government needs to work as a full partner with businesses, workers and communities". Lankin then listed several sectors as priorities for economic development – including construction, aerospace, autos, plastics, tourism and telecoms – and encouraged the federal government to work with Ontario in developing and funding strategies for each sector. Her main point was that "there are significant opportunities to improve business access to federal and provincial industrial

³⁸³ Archives of Ontario, Folder B501234 – CMIT March 18/93, "Briefing Note: Federal Prosperity Action Plan", 17 November 1992, p.3.

assistance programs”.³⁸⁴ The listing of sectors is evidence of Ontario’s desire to limit the topics of discussions based exclusively on a regional/provincial policy orientation.

The specific areas identified for reform are not unlike the areas of reform undertaken in Australia, including building linkages between a competitive domestic industrial base and overseas opportunities. The difference is that all Australian governments eventually accepted the need for a broadly-based reform programme. They committed because the economic crisis and ‘turn to Asia’ raised the stakes of failing to reform. Their commitment to the process began at the HoG level and was transmitted to ministers and sectoral negotiators via a whole-of-government approach to the SPC process of microeconomic and, eventually, IGR institutional reform.

In Canada, all were not agreed on the need for a comprehensive reform effort. Ontario did not accept Ottawa’s definition of what constituted a barrier to trade. The provincial government wanted to help business but not at the cost of its powers over the economy. The focus was on its own economic development rather than the strategic realignment of the economic union. Ontario wanted the reform process to occur within ministerial silos rather than be directed by a central agency such as the Premiers Office, which could organize a whole-of-government approach to the reform process. In all, Canada’s major sub-unit was championing a different programme than Ottawa, casting doubt on Ottawa’s reform agenda, process, and goals. In Lankin’s briefing note, the difference is stated clearly: “the CMIT should not be used to advance the federal government’s narrow interpretation of competitiveness which promotes trade

³⁸⁴ Archives of Ontario, Folder B501234 – CMIT March 18/93, “Minister’s Speaking Notes – Competitiveness,” 18 March 1993, p.1.

liberalization, deregulation of industry and reduction of government spending”,³⁸⁵ precisely the same items on Canberra’s list of reforms. Rather Ontario was seeking to be a full partner of business through direct funding, a position not unlike Victorian Premier Cain’s vision of economic development, which involved ‘picking winners’.

Whereas Victoria eventually joined the SPC process, Ontario was concerned that “the federal government is attempting to extend the mandate of the CMIT to include industrial development issues in the context of the federal competitiveness agenda”.³⁸⁶ Instead of expanding the CMIT’s mandate, Ontario believed that

increased federal-provincial cooperation in economic development issues would resolve many of the issues arising from counterproductive intergovernmental competition for investment...However, a number of provinces challenged the notion that limits should be placed on their ability to attract investment. Moreover, in most instances, Ontario competes directly against American states.³⁸⁷

Remaining competitive vis-à-vis American states could only be accomplished with Ontario fully exercising its sovereign powers. The goal was to both strategically support Ontario businesses and attract foreign investment. Some of the existing barriers were raised by other provinces and most of the others were the result of the legitimate exercise of its own economic powers. Its concern for its own regional development and competitiveness diminished its support for a national, comprehensive, and cooperative solution to Canada’s economic problems.

Despite Ontario’s skepticism, the March 1993 CMIT was a qualified success: Ministers committed “to proceed with a comprehensive negotiations process”. There were certain caveats

³⁸⁵ Archives of Ontario, Folder B501234 – CMIT March 18/93, “Background Briefing Note on CMIT: Competitiveness Issues,” 15 March 1993, p.1.

³⁸⁶ Ibid., p.2.

³⁸⁷ Ibid., p.3.

to the process: at the top of the list of “Principles to be respected during negotiations” was “provincial sovereignty” along with “transparency, national treatment”.³⁸⁸ Wilson was able to announce that negotiations would formally commence in July to secure an agreement in one year’s time (Knox, 1998, p. 143). Ultimate authority lay with HoG but Ministers were in charge of the actual process (Doern & MacDonald, 1999, p. 48). Concurrently, Ministers responsible for the labour market agreed to establish the Forum of Labour Market Ministers “which will set and implement an annual agenda of intergovernmental labour market projects...[such as] improving the way programs and services are delivered to clients and on simplifying the entry process of publicly-funded labour force development programs”.³⁸⁹ The *Globe and Mail* summarized all the developments: “the talks (announced March 18) are a good sign but given the progress thus far, an agreement is doubtful. The provinces remain reluctant to surrender their marketing boards, licensing, requirements and subsidies”.³⁹⁰

The good news story from the meeting was quickly followed by the “New Brunswick Government’s measures to keep Quebec construction firms out of [its] market. [The announcement] refocused media attention on the difficulties involved in the effort to eliminate trade barriers”.³⁹¹ As well, Wilson was unsure “that BC will see participation as either necessary or in the province’s basic interest”. Furthermore,

in the *Vancouver Sun*, BC Trade Minister David Zirnelt said his government would be willing to drop interprovincial trade barriers if the provinces can still set its own labour and environment regulations. ‘We want to...expand trade with Canada. But if the trade is so free that it means raw materials will flow

³⁸⁸ Archives of Ontario, Folder B501234 – Meeting: Chief Negotiators-Task Force of Officials on Internal Trade, “CMIT Meeting: Summary of Discussions and Decisions of Ministers,” 18 March 1993, p.1.

³⁸⁹ Archives of Ontario, Folder B501234 – CMIT March 18/93, “FTP Joint Communique,” [illegible] 1993, p.1.

³⁹⁰ Archives of Ontario, Folder B501234 – Meeting: Chief Negotiators-Task Force of Officials on Internal Trade, “Media Analysis March 18 CMIT Meeting for Internal Trade,” 2 April 1993, p.3.

³⁹¹ *Ibid.*, p.1.

to the industrial heartland, we would have to be cautious about the effects it would have on this region””.³⁹²

But BC would be alright if those same materials flowed to China instead? Like Ontario, BC was concerned about its own regional development and economic jurisdiction to the point that it was highly skeptical towards Ottawa’s reform agenda. As well, partisanship and perhaps even provincial jealousies were part of the reasons these provinces resisted the negotiations (each province’s individual political positions and political economies are more fully investigated in the next chapter).

With a full slate of negotiations announced, the co-chairs of the CMIT wrote to the other government departments at both the federal and provincial levels to inform them of the announced plan:

The purpose of this letter is to invite you, and the intergovernmental committee of which you are a part, to participate in the process of reaching a comprehensive agreement by undertaking negotiations to eliminate barriers and impediments to internal trade...Chief Negotiators have been named...They will coordinate the overall process and work on rules and compliance and other institutional mechanisms which would apply generally across all sectors.³⁹³

This was an attempt to create a whole-of-government approach at the bureaucratic level rather than at the political level. Chief negotiators for each jurisdiction were to report directly to their respective Internal Trade Minister and were collectively responsible for negotiations through a series of sector tables comprised of negotiators from each jurisdiction. Ontario raised the

³⁹² Ibid., p.2.

³⁹³ Archives of Ontario, Folder B510234 – CMIT June 7-8/93, “Letter from CMIT Co-Chairs to Federal Minister of Agriculture Mayer,” 24 June 1993, p.1.

concern that “the letter is not clear on how sectoral ministers are being invited to participate in the process”.³⁹⁴

In May, a report on the activities of other intergovernmental fora was prepared for Minister Lankin. Agriculture ministers were negotiating technical standards on food inspection and transportation. The more institutionalized Canadian Council of Ministers of the Environment (it meets twice a year and is supported by Deputy Ministers and a full-time secretariat) was working on a framework of cooperation on environmental issues. Other departments were meeting less frequently but were committed to establishing taskforces on internal trade issues.³⁹⁵ The important point is that each ministry believed it was best suited to tackling issues of standardization and harmonization within its own remit. At the moment, Internal Trade Ministers could only wait and see what their colleagues would negotiate in their respective policy areas.

The June 1993 CMIT meeting went ahead as scheduled, although Lankin was unable to attend. Wilson stated that “the world is becoming increasingly competitive...Internal trade barriers act as disincentives to trade and investment and lead to missed opportunities and lost jobs for Canadians”.³⁹⁶ Ministers “adopted an aggressive work program...to guide intergovernmental negotiations toward a successful conclusion of a Comprehensive Agreement on Internal Trade by June 30, 1994”. The comprehensiveness of the negotiations, i.e., the list of sectors up for negotiation, “is a useful starting point for negotiations, while recognizing that, once more detailed discussions are engaged, it may be appropriate to add sectors or issues for specific

³⁹⁴ Archives of Ontario, Folder B510234 – CMIT June 7-8/93, “Minister’s Briefing Note: CMIT Vancouver,” 7-8 June 1993, p.5. The archive file contains a draft letter prepared by BC that is identical to the addressed letters sent to various ministries.

³⁹⁵ Archives of Ontario, Folder B510234 – CMIT June 7-8/93, “Summary Other IG Fora Involved in Sectoral Internal Trade Issues,” 20 May 1993.

³⁹⁶ Archives of Ontario, Folder B510234 – CMIT June 7-8/93, “Press Release: Statement of CMIT”, 8 June 1993, p.1.

coverage” or to delete them from a comprehensive agreement.³⁹⁷ They also agreed that an independent chair would lead the process. Negotiations will proceed in three phases: 1) learning and understanding of the issues, which will involve “developing rules for internal trade that would give practical effect to the principles adopted by CMIT, thereby providing a framework for the discussion of sectoral issues”;³⁹⁸ 2) the construction of a draft agreement, ending with a ministerial review, and 3) negotiations to conclude the final agreement. However, Ontario approached the meeting concerned that “a number of the other provinces appear to have unrealistic expectations about how much can be achieved and do not appear to have considered how far this process should proceed”.³⁹⁹

Following the meeting, BC Minister Zirnelt stated that “our priority is jobs and economic development in our hard pressed resource regions...We want to ensure that we do not reduce internal trade barriers at the expense of the regions...We must not limit our capacity to pursue regional development.” He then released a study that was heavily critical of the CMA’s estimate that internal barriers were costing the economy upwards of \$6.5 billion. According to the new study, the costs were roughly \$700 million, or one-tenth the CMA figure (see Copeland, 1998). Zirnelt continued, “To me, these negotiations look more like pre-election posturing than a serious attempt to address real economic problems of importance to Canadians”.⁴⁰⁰ Saskatchewan officials also questioned reports that “suggested ‘huge’ benefits to the economy from eliminating internal barriers and said they hadn’t seen any evidence of the problem”. Knox

³⁹⁷ Archives of Ontario, Folder B510234 – CMIT June 7-8/93, “Report of Chief Negotiators to CMIT,” June 1993, p.2.

³⁹⁸ Ibid., p.1.

³⁹⁹ Archives of Ontario, Folder B510234 – CMIT June 7-8/93, “Minister’s Briefing Note: CMIT Vancouver,” 7-8 June 1993, p.5.

⁴⁰⁰ Archives of Ontario, Folder B705175 – Communications: Other Provinces, “News Release: Zirnelt says regional issues paramount during internal trade talks,” 7 June 1993, p.1.

dismissed these concerns. BC negotiator Dave Morel added that “there was no ‘ground swell’ of lobbying activity by interest groups in BC on internal barriers. He made the point that there needed to be some compelling reasons for the inclusion of sectors in the negotiating process”. When Knox was pressed by Wright that she “had seen little evidence from our industry that they were concerned about internal trade barriers,” Knox responded “that federal consultations...had shown that this was a serious problem and ‘many’ sectors and labour(??) [sic] had approached Minister Wilson. Bob [Knox] mentioned auto and railways”.⁴⁰¹ In the end, Knox was supported by officials from Newfoundland, Nova Scotia, and Alberta, each of whom was ready to “go to their cabinets without a clear notion of what was being negotiated”. Québec responded that it was “in the ‘process of setting up a process’ to deal with the internal trade issue”.⁴⁰²

Concerns regarding internal barriers did exist and they came from BC. At a meeting of Agricultural Ministers, BC’s Bill Barlee stated that cross-border shopping, at an exchange rate of 80 cents to the USD, was particularly concerning since it amounted to a loss of \$500 million of food product sales. It wanted provincial and federal governments to establish national standards, with strong national trade and a market development strategy.⁴⁰³ The contrast between Zirnhelt and Barlee is interesting. On the one hand, BC was resisting AIT negotiations on the basis of supporting its regional economy and because of the purported paltry savings for the national economy. On the other hand, BC wanted a national strategy to support its food industry. BC, like

⁴⁰¹ Archives of Ontario, Folder B501234 – Meeting: Chief Negotiators-Task Force of Officials on Internal Trade, “Email from Wright to Katherine McGuire [Director of ON Trade Policy Branch]: The comprehensive process begins,” 18 December 1992, p.2.

⁴⁰² Ibid., p.3.

⁴⁰³ BAnQ Montreal, z2-830-484-037, “1993 Federal-Provincial-Territorial Conference of Ministers and Deputy Ministers of Agriculture,” 7 July 1993.

Ontario, was concerned about its own competitiveness and looked to cooperative solutions only on a case-by-case basis.

Canada's 'Closer Partnership' Moment?

On 6 August 1993, Deputy PM and Industry Minister Jean Charest announced Arthur Mauro's appointment as Chair of the AIT negotiations: "His background, in investment, transportation and communications, makes him uniquely qualified".⁴⁰⁴ According to Charest, "He will take any actions required to facilitate progress...[he] will help keep the negotiations on track".⁴⁰⁵ He also stated

the process that is now underway is a national process, not a federal one. I say this because its success to date has been due in large part to the collaboration of the provinces between which these barriers stand. I am also pleased that the federal government has been able to play a leadership role in facilitating the establishment of the process.⁴⁰⁶

The AIT was supposed to be not only a domestic economic reform effort but a different way of conducting IGR in Canada. The constitutional negotiations and Mulroney's resignation had forced Ottawa to consider a different approach. Rather than have the PM chair the negotiations, and inject partisanship and politics into the process, a neutral chair was sought to provide a non-partisan and expert voice to the negotiations. Federal negotiators were to be active participants but for the first time they were not to overtly control the negotiating process. Wilson had previously stated his preference for a neutral third party to chair the negotiations, "someone

⁴⁰⁴ Archives of Ontario, Folder B705175 – Communications: Canada, "World Report: CBC Radio," 6 Aug 1993, p.2.

⁴⁰⁵ Archives of Ontario, Folder B705175 – Communications: Canada, "Notes for an Address by Minister Charest to the Winnipeg Chamber of Commerce," 6 August 1993, p.7.

⁴⁰⁶ Ibid., p.8.

with private sector experience”.⁴⁰⁷ At the CMIT, Ottawa indicated it wanted “a high-profile third party who will take an active and public role in driving the negotiations forward”.⁴⁰⁸ Upon his appointment, Mauro was quoted in the *Financial Post* as saying “that [an agreement is] an imperative in the marketplace that we find ourselves in today...I think there is the will out there to do it. It is not a partisan issue”.⁴⁰⁹

Thus, Ottawa was willing to sit as an equal with the provinces and not retain the powers of chair. The decision to appoint a neutral chair helped to launch the AIT negotiations. It also signalled a passing of the leadership baton from HoG to their Ministers and technocrats. Internal trade was important but without the inclusion of fiscal federalism, perhaps it was not *that* important. What was important was whether or not provincial authority was respected: “[Ontario] was not convinced such a position is necessary for a successful outcome...If there is to be such a position, it should be a low-key facilitative role”.⁴¹⁰ It thought the chair “would preempt the role of Ministers in directing the comprehensive negotiations...[and] that the proposed Chair will not be an ‘honest broker’ of differing federal and provincial interests”; it believed it had the support of BC,⁴¹¹ Saskatchewan “and perhaps Quebec”.⁴¹² Interestingly, Lankin’s list of suggestions for chair was composed mostly of professors of political science, including Dupré,

⁴⁰⁷ Archives of Ontario, Folder B501234 – Meeting: Chief Negotiators-Task Force of Officials on Internal Trade, “Notes from Conference Call: Task Force of Officials on Internal Trade,” 26 March 1993, p.1.

⁴⁰⁸ Archives of Ontario, Folder B510234 – CMIT June 7-8/93, “Minister’s Briefing Note: CMIT Vancouver,” 7-8 June 1993, p.3.

⁴⁰⁹ Archives of Ontario, Folder B501234 – Meeting: Chief Negotiators Sept 1-2/93, “Provincial barriers under siege,” *Financial Post*, 6 August 1993.

⁴¹⁰ Archives of Ontario, Folder B510234 – CMIT June 7-8/93, “Letter from Lankin to Wilson,” 7 June 1993, p.2.

⁴¹¹ The letter from BC states that the Chair “would not allow for balanced representation of the different views and priorities of the provinces...nor would such a structure follow the format for international trade negotiations, such as the NAFTA, that the federal government has indicated it wishes to follow” (Archives of Ontario, Folder B510234 – CMIT June 7-8/93, “Letter from BC Deputy Minister McKinnon to Fed Deputy Minister Swain,” 23 April 1993, p.1).

⁴¹² Archives of Ontario, Folder B510234 – CMIT June 7-8/93, “Memo from ON Deputy Minister Peter Barnes to Lankin,” 22 April 1993, p.1.

Simeon, Cameron, and Swinton; the rest were former deputy ministers.⁴¹³ The professors were listed in particular because Ontario wanted “someone who understands the constitutional role of the provinces and, in particular, the responsibilities of provincial governments for economic development”.⁴¹⁴

A day after announcing Mauro’s appointment, Charest stumped for the negotiations. Charest answered a question from CBC Radio about on his role as Industry Minister by referring to the need to commit to the upcoming internal trade negotiations:

...there are issues like internal trade barriers, where my department plays a key role...So the difference...will have to be in the commitment, the very clear commitment by governments, to a process and to a time frame...[P]rotectionism will make us less competitive, reduces the market share that we have with technological innovation, with competitiveness, the real growth in jobs, the potential growth in jobs for us resides first in increasing market share...Now, that’s the reason why we put such a strong emphasis on the trade issue, because that is the way we create jobs in this country. And if it’s true of other countries, well, boy, from my point of view, it has to be true within Canada”.⁴¹⁵

Then, on 27 August, the Premiers met in Nova Scotia. They agreed a ‘FMC on the Economy’ should be held soon after the upcoming federal election. They also called on Economic Development and Finance Ministers “to study ways of working together to promote job creation in all regions of Canada,” with a particular nod to the link between infrastructure investment and overall economic development. “[First Ministers] believe that not only must the federal government avoid making cuts to transfer payments, but governments must cooperate to reform the transfer payments programs, and fiscal arrangements, as soon as possible”.⁴¹⁶ Thus, enough

⁴¹³ Archives of Ontario, Folder B510234 – CMIT June 7-8/93, “Letter from Lankin to Wilson,” 21 May 1993, p.1.

⁴¹⁴ Archives of Ontario, Folder B510234 – CMIT June 7-8/93, “Memo from Barnes to Lankin,” 22 April 1993, p.3.

⁴¹⁵ Archives of Ontario, Folder B705175 – Communications: Canada, “The House: CBC Radio,” 7 August 1993, p.1.

⁴¹⁶ Archives of Ontario, Folder B705175 – Communications: First Minister, “Final Communiqué: 34th Annual Premiers’ Conference, Baddeck, NS,” 27 August 1993, p.1. Western Finance Ministers also called for new fiscal

political will existed to commit to and perhaps expand the economic reform negotiations. Premiers hoped “a comprehensive reform process should integrate the work of Finance Ministers and be done at the direction of First Ministers”.⁴¹⁷

The provinces’ desire to “integrate the work of Finance Ministers” into a reform programme mirrors the Australian states’ demand to reform fiscal federalism along with internal trade. Yet Ottawa was not as open to the idea as Canberra. The fiscal issue had an impact on Campbell’s attempt to host consultations with Premiers before the July 1993 G-7 summit in Tokyo. At the consultations, Ontario was notably absent.⁴¹⁸ As one former senior government official stated, it was viewed as an election stunt; it was merely “a TV show”. The real reason for not attending was because the federal government was refusing to negotiate on fiscal federalism or social programs.⁴¹⁹ The disagreement is contained in an exchange of letters between Campbell and Rae. Just prior to the Premiers’ meeting, Rae wrote Campbell to “insist that the federal government not make any more ad hoc arrangements, pursue any more negotiations in secret, or conclude any further deals that are not based upon multilaterally-agreed principles respecting fairness in the allocation of federal training funds”.⁴²⁰ Campbell replied that HoG should “begin a targeted process of rationalizing the delivery of programs and services, cutting ‘red tape’, improving accessibility and enhancing coordination in a number of important areas, such as

arrangements at the 32nd Annual Premiers’ Conference (see Ottawa, “32nd Annual Premiers’ Conference, documents: Report of the Western Finance Ministers, 13-14 May 1991”).

⁴¹⁷ Archives of Ontario, Folder B353188 – Premier’s Conference – 1993, “Letter from Ralph Klein to Kim Campbell,” 23 August 1993, p.1.

⁴¹⁸ NFLD Premier Wells was also absent because of a delayed flight.

⁴¹⁹ Interview with former senior provincial government official, 26 August 2015.

⁴²⁰ Archives of Ontario, Folder B368296 – Correspondence with Kim Campbell, “Letter from Rae to Campbell,” 5 August 1993, p.2.

environmental assessment and regulations".⁴²¹ Rae replied that he supported a cooperative reform effort but "cooperation cannot be built or sustained without fairness". The unfairness was that Ontario had 37% of national unemployment yet received only 27% of federal training funding.⁴²²

Between July and late August 1993, Campbell took a new tack with the provinces. On the same day as the Premiers' meeting in Nova Scotia, she spoke to the Rotary Club of Toronto. Her speech, under different circumstances, could be considered on par with Bob Hawke's 'Closer Partnership' speech. In it she essentially outlined that Canada is also a 'lucky country':

For decades, our Canadian capacity to produce wealth was unquestioned...We could count our competition abroad on one hand...It seemed as if we would coast on, a country of comfort on cruise control...Well, if we ever could coast, we can't coast now...The choice is clear: to either lead change or have change leave us behind.

In the lead up to the 1993 election – writs were dropped just over a week after this speech – Campbell was going to be "frank" with Canadians:

What won't work is trying to put walls up around Canada...What won't work is acting as if government alone can or should solve the country's economic problems...I believe that Canada's national government has three broad economic responsibilities...to create the framework for economic opportunity,...to help Canadians succeed within that framework,...[and] to bring Canadians together in partnership...What this country needs is a new economic partnership involving every sector, every level of government in Canada.⁴²³

⁴²¹ Archives of Ontario, Folder B368296 – Correspondence with Kim Campbell, "Letter from Campbell to Rae," 2 September 1993, p.3.

⁴²² Archives of Ontario, Folder B368296 – Correspondence with Kim Campbell, "Letter from Rae to Campbell," 5 October 1993, p.1.

⁴²³ Archives of Ontario, Folder B705175 – Communications: Canada, "Notes for an Address by Campbell to the Rotary Club of Toronto," 27 August 1993, p.1.

The similarities between Kim Campbell's speech and Bob Hawke's are striking. In the same time period, the early-1990s, both Canada and Australia arrived at a similar moment of economic truth: that liberalization and intergovernmental cooperation were the pathway to a more prosperous future, which only a more competitive and efficient economy could achieve. Campbell's plan would begin by tackling the deficit:

During my meeting with the Premiers before the G-7 Summit, we began a dialogue on how to address together our common challenges on taxes, on spending, on deficits. I intend to pursue that dialogue vigorously. Within 30 days of the upcoming election, I will convene a First Ministers' Meeting to pursue discussions on a National Debt Management Plan....[One of the] four cornerstones to a workable plan...[is] a collective effort to eliminate waste and duplication, both within and between governments...I believe the country's governments must come together to look closely at what government does, at what Canadians expect their governments to do, and at what level of government should do it.⁴²⁴

Just like Hawke, Campbell was signalling that the federal government was open and ready to negotiate on fiscal federalism and on duplication and overlap. Campbell recalled the July consultations in her memoir:

I was struck by the consensus among the premiers present, who represented all three major Canadian political parties...I was inwardly very encouraged that there was, indeed, an opportunity to 'de-partisanize' the issue. Most surprisingly, and gratifying, to me was that they didn't gang up on me, but talked constructively about the problems...[W]e all knew how tough the challenges facing us were, and I could see that the premiers recognized the political credit that a more consensual approach could now bring (Campbell, 1996, p. 328).

The recession and advent of free trade appeared to crack open a window of opportunity to negotiate on the major issues facing the country. The deficit issue had confounded Canadian governments in the past. The increase in the federal deficit from \$14.6 billion in 1981 to \$39

⁴²⁴ Ibid., p.3.

billion in 1993 pushed Canada's total debt-to-GDP ratio up to 68.4% (and that figure did not include provincial and municipal debt) (Veldhuis et al., 2012). As in Australia, alarm bells were starting to go off. And like in Australia, leadership was also a factor. According to Campbell (1996, p. 326),

because I had served at all three levels of government, I understood the challenges facing provincial governments and had considerable sympathy for them. I believed that a clear demonstration that the federal government would no longer act unilaterally in ways that heavily affected provincial areas of responsibility could make for a fairer federalism.

Campbell's speech has several parallels to Bob Hawke's 'Closer Partnership' speech, including economic reform and recognizing that success required intergovernmental cooperation on many issues, including fiscal transfers. But its political timing was very different. Hawke's call to action came on the heels of his record fourth election victory; Campbell's Progressive Conservatives would not be so fortunate. Despite her promises and bold vision, progress on the economic front was too slow to assist the Party at the polls in October. After nine years in power, two failed constitutional negotiations, a splintering of the party, the resignation of the PM, and a few gaffes during the campaign, the Progressive Conservatives lost 154 seats. With only two seats in the 35th Parliament, it was their worst showing since Confederation.

Would PM Campbell have carried through with her promises? It is an almost impossible counterfactual but there are a few hints of what might have been. In her speech announcing her run for the Progressive Conservative Party leadership Campbell spoke of provincial aspirations in her home province: "British Columbians in general tend to be visionary, forward-looking, energetic, enthusiastic, very entrepreneurial. We feel that our future is still in front of us, not behind us, and we're willing to try new things. But we also have a sense that from time to time

the government of Canada doesn't serve us well" (Campbell, 1996, p. 267). She also stated that "my approach to the use of power was dramatically different from what was customary in the federal government...My commitment to involve the provinces in making policy that affected their responsibilities...[was] designed to make it possible to create the support necessary to tackle the deficit both seriously and sensibly" (ibid., p.346). During the federal election campaign, Campbell contrasted the Liberal Red Book's promise of \$6 billion in infrastructure spending to the Progressive Conservative plan to create jobs through microeconomic reform: "we wanted to focus on retraining workers, promotion of small business, promotion of the commercialization of Canadian innovation in Canada, reducing the administrative and financial burden of government on business, and promoting export markets" (ibid., p.356). Hindsight is 20/20 but the sentiment and policy proposals are so similar to Hawke's as to make one wonder what might have been.

The new government of Liberal PM Jean Chrétien in fact continued the economic reform effort of the Progressive Conservatives, with Industry Minister John Manley giving it high priority. There are several reasons for this, the first of which begins at the top: pursuing an improved Canadian economic union had been on Chrétien's agenda since his tenure as Minister of Constitutional Affairs in 1980 (Leeson, 2000, p. 9). The remaining reasons are largely economic in nature, particularly the ongoing recession. These reasons also help explain the Liberal Party's about-face on free trade and liberalization soon after Chrétien won the Liberal Party leadership in June 1990. At a party political conference in Aylmer, QC in November 1991, "most of the speakers were proponents of a deficit-free, open-border ethos. Their argument was that since globalization was inevitable, there was no use trying to hide behind old-fashioned protectionism. Chrétien came to the conference prepared to accept the new thinking" (L. Martin, 2003, p. 47).

Yet the two political parties were intense competitors. During the debates over the FTA, Chrétien warned it would draw Canada “into an ever-narrowing economic corridor...‘And then Canada as a country would disappear’. There might be economic advantages to free trade, but there was more to life than the bottom line. ‘I know,’ said Chrétien, ‘that Canadians are willing to pay a price to be Canadian’” (ibid., p. 371). But that was only half the problem. Mulroney’s support for Meech Lake coupled with free trade gave Chrétien “a potent oversimplification. ‘Mulroney,’ he said, ‘gave half the country away to the provinces and the rest to the US’” (ibid., p. 372). According to long-time advisor David Zussman, “‘I think he’s a centralizer’...‘He sees a very vigorous role for the federal government’” (ibid., p. 59). Chrétien was not offering the same cooperative spirit as Campbell.

Without specific political impetus from HoG, the decentralized, sector-based negotiating progress was proceeding slowly. Its decentralization was specifically noted in a briefing to Lankin: “we have adopted a decentralized process in these negotiations and that Trade Ministers should not attempt to direct the work of their colleagues with respect to matters of the details and timing of their efforts to address internal trade barriers in their sector”.⁴²⁵ In fact, Ontario expected “to continue to use bilaterals after an internal trade agreement has been reached because many issues will not be sufficient importance to all parties to merit a multilateral deal”.⁴²⁶ Decentralization was causing confusion. Labour mobility negotiators had only met for the first time in November 1993 and reported “considerable confusion and disagreement among jurisdictions with respect to the proposed Articles and over the intentions of the Chief

⁴²⁵ Archives of Ontario, Folder B501234 – CMIT-June 6-7/94, “CMIT Fredericton: Meeting Scenario Note,” 3 June 1994, p.4.

⁴²⁶ Ibid., p.15.

Negotiators”.⁴²⁷ This perception was confirmed by NB Chief Negotiator Wheatley, who was the only chief negotiator at a natural resources sectoral meeting:

During some of the discussion there appeared to be a lot of confusion and general lack of focus on what the Chief Negotiators are looking for in terms of draft agreements and the discussion on their particular sector...Secondly, a lot of concern was expressed with respect to the overlap between issues related to that particular sector and issues being discussed by other sector groups.⁴²⁸

To mitigate the confusion, a draft set of general rules was distributed to the sectoral negotiators since “[it would allow] them to report back on how they could be applied to their sectors...[since] the entire focus of the sector talks will be on exceptions, rather than finding mutually beneficial commitments”.⁴²⁹

Political impetus was finally injected when Chrétien, facing “difficult economic and fiscal circumstances...convene[d] an informal meeting of First Ministers...on December 21, 1993”.⁴³⁰ No communiqué was issued but an agreement was reached on splitting the cost of a national public works program (Poels, 1994). Chrétien wrote to Rae beforehand that he wanted to “achiev[e] a balanced and cooperative approach to economic renewal and fiscal responsibility, promoting job creation and a competitive economy, and enhancing service to Canadians through improved program coordination”.⁴³¹ The day after the FMM, Finance Minister Paul Martin fired Bank of Canada Chief John Crow, who resisted the idea of curtailing interest rates in an attempt

⁴²⁷ Québec Archives, Box 24 A 001 09-04-003B-01, File 2005-10-003\271, “Comments from the Sectoral Table on Labor Mobility,” 19 January 1994, p.2.

⁴²⁸ Québec Archives, Box 24 A 001 09-04-003B-01, File 2005-10-003\271, “Letter from NB Asst Deputy Minister Wheatley to Arthur Mauro,” 19 January 1994, p.1.

⁴²⁹ Archives of Ontario, Folder B501234 – Text-Draft Framework Agreement & Descriptive Companion-Oct-Nov/93, “Memorandum from ON Asst Deputy Minister Sadlier-Brown to AB Deputy Minister Thumlert,” 24 Sept 1993, p.1

⁴³⁰ Archives of Ontario, Folder B368296 – Correspondence with Jean Chrétien, “Letter from Chrétien to Rae,” 29 November 1993, p.1-2.

⁴³¹ Ibid.

to end the recession. Canada too was having the 'recession it had to have' that would kill inflation but, in the meantime, it was also killing jobs, growth, and adding to the deficit (L. Martin, 2003, p. 81). With the macro-economy in trouble, Ottawa had no choice but to continue with microeconomic reform. Like Hawke, Chrétien was forced to act because of external economic pressures.

On Christmas Eve 1993, Manley presented to Cabinet a memorandum on the internal trade negotiations. The issue before Cabinet was on how to proceed with the ongoing negotiations. The Liberals committed to the previous government's timetable as well as to the desire for a comprehensive, transparent, rules-based approach to internal trade.⁴³² However, at this stage Manley recognized that "it will not be possible within the current timetable to conclude as broad and deep an agreement as originally outlined". The reasons were two fold. Manley placed part of the blame on certain provincial governments, "notably Ontario and British Columbia", who were using unspecified delaying tactics.⁴³³

The rest of the blame was on the structure of the negotiations: "Certain elements of the negotiations which rely on progress by other groups of ministers and their officials...cannot be concluded in the time available given often competing priorities".⁴³⁴ Meanwhile, Ottawa was moving forward on issues within its jurisdiction: "The infrastructure initiative, the re-direction of income security programs, the financing of small and medium-sized enterprises, the focus on technology and innovation are illustrative [of the government's focus] on building the

⁴³² PCO FOI request (A-2014-00381/JL): Doc. 3-0002-94MC(01), 24 December 1993, "Memorandum to Cabinet: Intergovernmental Negotiations on Internal Trade," p.3.

⁴³³ Ibid., p.5.

⁴³⁴ Ibid.

frameworks for an integrated competitive domestic economy in order to increase Canada's ability to compete internationally".⁴³⁵ But a broadly-based reform programme required the cooperation of the provinces. Without HoG directly steering the process, multiple reform efforts remained siloed in their respective ministries and jurisdictions, preventing a whole-of-government approach from emerging to deal with the mechanism of continuous negotiations, thus limiting the mechanism's ability to expand the negotiations beyond economic reforms.

Manley believed that a rules-based agreement could be agreed via a process of multiple rounds of negotiations rather than in one round. Part of the reason was because several provincial efforts to remove or get around barriers had created a "patchwork of disparate outcomes, with idiosyncratic coverage, exceptions, and dispute resolution mechanisms,"⁴³⁶ which were adding to the problem of a balkanized economy, not solving it. The Australian SPC process comprised of multiple negotiating rounds was clearly better able to manage recalcitrant state governments. It was also better able to engage a whole-of-government approach with HoG that included all relevant policy areas, which ultimately helped seal package deals on reforms in order to achieve a truly integrated domestic economy.

Having acknowledged the problems, Manley concluded that because significant progress had already been made, Ottawa should continue to push for a "good, comprehensive framework agreement". Doing so would open a window of opportunity for further rounds of negotiations: "an early tangible success on the intergovernmental front would demonstrate to Canadians that governments can work together to solve difficult problems, and it would set an important

⁴³⁵ Ibid., p.17.

⁴³⁶ Ibid., p.13.

cooperative tone for a much more extensive intergovernmental agenda". Once a deal was agreed,

we could continue with more detailed negotiations on specific sectors and on the comprehensive elimination/phase out of incompatible measures. This schedule would give cabinet colleagues more time to plan for their respective negotiations. The two-step approach would also make room...for some provincial governments, notably Ontario and Quebec, to hold general elections.⁴³⁷

Clearly a second round would be needed since, thus far in the negotiations, "the question of subsidies/economic development has not yet been addressed".⁴³⁸ Such issues could be dealt with over the course of a multi-tiered negotiating strategy, whereby "staging the negotiations and the agreement itself into related phases gives governments additional flexibility over the degree and pace of market integration. It also allows governments to set aside issues that are particularly intractable to later in the process".⁴³⁹

Whether or not the first round would even succeed would be decided at the next CMIT meeting on 20 January 1994. At this meeting, the federal and provincial governments needed to decide again on the kind of agreement they wanted to complete: a rules-based approach to all internal trade or a sector-by-sector agreement that only sought to remove specific barriers and impediments. Whatever occurred, Manley wanted all parties to at least agree to "carry on with phase two on a specific time track and with clearly articulated objectives".⁴⁴⁰

Despite Manley's proposal for multiple, tiered rounds of negotiations, certain provinces "such as Ontario, will explicitly or implicitly link progress on the internal trade front with federal

⁴³⁷ Ibid., p.5.

⁴³⁸ Ibid., p.19.

⁴³⁹ Ibid., p.21.

⁴⁴⁰ Ibid., p.7.

concessions in other areas subject to federal-provincial negotiation". Manley concluded that this was the real reason behind Ontario's reluctance, especially since it was the province that had the most to gain from opening internal trade. Manley's response to this issue is perhaps the biggest missed opportunity of the AIT: "the Government will need to resist linkages".⁴⁴¹ According to one former senior government official, keeping the most important issue, fiscal federalism, off the table emanated from Deputy Finance Minister David Dodge, present during both Progressive Conservative and Liberal governments, who was "stubborn" and refused to address fiscal federalism cooperatively in a multi-lateral forum.⁴⁴² The desire to retain Ottawa's spending power continued even after the AIT: "Ottawa deliberately avoided committing itself to a more collaborative approach as jointly requested by the provinces at the end of the 1990s and largely ignored even the moderate restrictions on the federal spending power as they were provided for in the SUFA" (Broschek, 2010, p. 17). Whereas unilateralism caused the 1990 Premiers' Conference dust up in Australia, no such provincial revolt was witnessed in Canada. Rather, the provinces simply chose to go it alone.

The result prevented a package deal on a broad set of issues that could have achieved significant reform and IGR institutional change. According to the Manley memorandum, such a linkage was not necessary because the negotiations were on a fast track and internal trade contained "sufficient scope through a comprehensive internal trade negotiation for trade-offs within the overall package, without having to look elsewhere for balance. The key to resisting linkage will be to maintain public pressure on the provinces...for a good agreement on its

⁴⁴¹ Ibid.

⁴⁴² Interview with former senior provincial government official, 26 August 2015.

merits”.⁴⁴³ This is despite the memorandum’s acknowledgement that “duplicative or unnecessary government administrative and regulatory structures” were a drag on the economy⁴⁴⁴ and its observation that internal trade negotiators were waiting for the other ministries to complete negotiations.

Several other former government officials noted that internal trade was simply too small an issue to link with the much larger and more politically salient issue of federal-provincial transfers, a major component of Canadian fiscal federalism. Given that the internal trade issue had already been fragmented in terms of sectoral areas, the decision not to link issues makes some sense. However, after taking into consideration all the policies that directly impact upon the economic union but were not included in the AIT, such as R&D, labour training, etc., it does seem possible that a wider range of economic issues could have been linked with fiscal reform. At least, they were in Australia. In Canada, the idea was floated at the provincial level but Ottawa was not interested. The cost would be the effectiveness of its internal trade and intergovernmental reform agenda.

Conclusion

Events and trends in public policy converged in the early-1990s to encourage microeconomic reform. Decades of regional/provincial specialization behind the tariff wall and a reliance on foreign trade had balkanized the Canadian domestic economy to the point that it was unprepared for the rigors of free trade. Falling competitiveness and productivity combined with

⁴⁴³ PCO FOI request (A-2014-00381/JL): Doc. 3-0002-94MC(01), 24 December 1993, “Memorandum to Cabinet: Intergovernmental Negotiations on Internal Trade,” p.7.

⁴⁴⁴ Ibid., p.13.

rising deficits and the abandonment of the national policy orientation sent policy-makers scrambling for solutions. When constitutional negotiations failed, leaders had no choice but to turn to their IGR system.

At HoG summits in March 1992 and December 1993, leaders launched the mechanism of continuous negotiation on microeconomic reform through Ottawa's proposal for a comprehensive deal on internal trade. Yet Industry Minister Manley was in need of some advice from now-retired PM Bob Hawke. Hawke had experience in getting sub-units to support a reform effort by offering to discuss other areas of federal-provincial concern, particularly fiscal federalism. Australia's economic situation – the urgency of the crisis and the risk inherent in the 'turn to Asia' – helped open a window of opportunity for actors to commit to and agree on the necessity of reforming both the economy and IGR decision-making. Getting them to step through it was enhanced by Hawke's genuine willingness to reset the relationship with the states and engage on all policy areas of concern to both orders of governments. By doing so, COAG was founded.

In Canada, the mechanism of continuous negotiations was launched to deal with Canada's own economic situation. Discussions were also occurring on controversial issues such as fiscal transfers, economic development, and duplication and overlap in government services. Ottawa had long committed to internal trade reform but was unwilling to expand the process to include fiscal federalism. The provinces expressed their desire to reform fiscal transfers as well as the economy yet they were skeptical of Ottawa's plan to reform only internal trade via a comprehensive, rules-based agreement. Why did actors behave in ways that ultimately placed limits on the very mechanism of continuous negotiation that they themselves engaged?

The next chapter more fully outlines how Canada's concentrated external market integration incentivized non-cooperative behavior, which included a focus on provincial sovereignty and regional development as well as a lack of engagement on the part of HoG. The risk of not reforming was lower in Canada than in Australia owing to the recently completed FTA, whereby Canada had secured its access to its most important trading partner. Committing to a reform programme that would radically alter the governance of the economic union became less urgent. Ottawa was not pressured nor desperate enough to place fiscal federalism on the agenda and the Premiers were unconvinced that reforms to internal trade and intergovernmental decision-making were their only options. In Australia, the urgency and risk emanating from its political economy – construed as the economic crisis and 'turn to Asia' – convinced HoG to take a leap of faith that Canadian leaders were also considered yet ultimately did not fully act upon. It was an opportunity lost.

Considering that in a few short years Ottawa would unilaterally cut transfers to the provinces, there was clearly a missed opportunity to create a process by which Canada's economic difficulties, reform effort, and debt problem could have been tackled collaboratively rather than unilaterally. At the time of Manley's memorandum to Cabinet, the deficit was a known problem:

In the wake of the recent announcement from the Minister of Finance [Paul Martin] regarding the potential extent of the deficit, it is clear that it is time for government to move on the economic front. Canadians have consistently voiced the view that government spending must be reduced and governments at all orders must begin to cooperate more effectively to reduce the load on taxpayers in this country.⁴⁴⁵

⁴⁴⁵ Ibid., p.41.

Why was a broadly-based reform effort not pursued? For one, the Liberals were a brand new government tackling a whole host of issues, only one of which was internal trade. Also, when the Australian SPC process began, there was an 18-month gap of no scheduled elections during which real progress could be achieved before partisan posturing reemerged. In Canada, as Manley mentioned specifically, the election window was significantly smaller and more pressing owing to the recently failed constitutional accords and the rising popularity of the Parti Québécois. On internal trade, Ottawa could at least reach an agreement however minimal rather than preside over yet another failed federal-provincial effort to conclude significant reforms. There were also partisan considerations, since it is likely that the federal Liberals were not on the same wavelength as Bob Rae's NDP nor the other provincial NDP or Progressive Conservative governments, and vice versa. Thus the partisan variable does play a role, as it did in Australia,⁴⁴⁶ but its specific effects remain tangled up with the other issues. As the Manley memorandum stated, the deep recession in the early-1990s, "lingering high unemployment and the fiscal straitjacket...have given voice to protectionist sentiments in some provinces".⁴⁴⁷

Nevertheless it is clear that the mechanism of continuous negotiation engaged on the internal trade issue, opening a window of opportunity for IGR institutional change. The Australian case demonstrates that, despite certain pitfalls, one the main determinants of HoG summit institutionalization is the political economy. In the Manley memorandum, the reasons why Canada needed a reformed internal market were discussed: globalization and trade liberalization

⁴⁴⁶ In Australia, there was no third governing party present. Nevertheless, the Australian Labor Party is akin to the NDP in terms of ideological origins yet it is similar to Canada's Liberals in that Labor occupied the centre and remained electable.

⁴⁴⁷ PCO FOI request (A-2014-00381/JL): Doc. 3-0002-94MC(01), 24 December 1993, "Memorandum to Cabinet: Intergovernmental Negotiations on Internal Trade," p.13.

in the 1980s and early-1990s had created a situation whereby industrialized economies were now competing directly with each other for investment. Such competition “hinges on the attributes and infrastructure of [the] internal market”. Liberalization was also putting Canadian producers in direct competition with international producers on Canadian soil, essentially blurring the lines between domestic and foreign trade. Finally, it was admitted that the FTA and upcoming NAFTA agreement could enhance north-south trade to the detriment of the economic union itself.⁴⁴⁸ “The elimination of barriers and impediments to trade is thus a competitiveness issue. Yet, at its core, it is also about the economic union – re-defining federal-provincial relationships in order to build and sustain a dynamic economy”.⁴⁴⁹ Therefore, with all the pieces for a successful institutionalization in place, it remains now to consider why the window of opportunity for IGR institutional reform closed.

⁴⁴⁸ Ibid., p.11.

⁴⁴⁹ Ibid., p.13.

Chapter 6:

Why the AIT failed to institutionalize FMCs

*I have participated through [Charlottetown], as I participated through Meech Lake. I must say that you get a sense of the magnificence of this country but also of the extreme complexity of it.*⁴⁵⁰

Donald Ross (Don) Getty
Premier of Alberta, 1985-1992

⁴⁵⁰ BAnQ Montreal, CE32-X7 1992 doc.8 cof, "First Ministers' Meeting on the Constitution: Evening Press Conference," 28 August 1992 (Doc 800-032/010).

Armed with the reasons why the AIT process was engaged and how it was structured, the following chapter analyzes the negotiations as they proceeded from the beginning of 1994. It starts by examining each province's position on internal trade and their economic and political circumstances. Canadian provinces were divided into two general camps with regard to internal trade: either they supported the AIT as the route to regional development via increased competitiveness and investment or they concerned the AIT could prevent direct government intervention in the economy. What conditioned provincial positions? The story cannot be told without examining their political economies. Most provinces supported international free trade yet were opposed to opening internal trade. The provinces wanted to maximize their gains from external trade in the name of regional development, which in turn caused actors to seek maximal policy independence and to harbour skepticism towards efforts at cooperation and coordination. Partisanship partly explains provincial negotiating positions and, in the literature, the partisan aspect has received the majority of attention, particularly with regard to the politics of Québec and Ontario. The following seeks to include the role of the political economy in conditioning actor behaviour towards a cooperative reform effort.

The political economy incentive as exemplified by the issue of regional development curtailed the AIT negotiations. Concentrated external market integration incentivized competitive behaviour between provinces over and above national economic reforms. A comprehensive, rules-based internal trade agreement was opposed to the more immediate goal of regional development. The provinces' desire for policy independence to manage their economic development and exposure to USA free trade and competition translated into an unwillingness to cooperate. Few provinces remained ideologically consistent on these issues,

highlighting the significance of other variables. Even Bob Rae's NDP – who maintained for so long their partisan opposition to all free trade agreements – compromised to reach a deal owing to Ontario's central position in the Canadian economy; even the most ideological government could not resist the pull of economic and historical factors. When the AIT was finally signed in July 1994, it remained incomplete. Further negotiations to expand and deepen it were prolonged, achieved mixed success, and became less of a priority. The mechanism of continuous negotiation was poised to expand to include institutional reform but, in the end, that effort was thwarted.

The View from the Provinces

Suffice it to say that regarding internal trade the provinces were less than enthusiastic. As Gherson (1994) summarized, “most of the provinces had to be dragged to the bargaining table in the first place, unconvinced that trade barriers were really so bad. Once there, they dug in defensively”. One former senior government official commented that the internal trade file was a “hodge podge” of issues and the real barrier, supply management, was not on the table.⁴⁵¹ Additionally, the barriers identified for removal were quite technical in nature, which allowed interest groups to pressure provincial ministries, helping to slow the progress of reform to a “glacial pace”. Interest groups “tell politicians to use their sovereign powers instead of letting them fade away. Each jurisdiction can intervene and do so legitimately”.⁴⁵²

The general division of provinces into two camps can be refined further. D. Brown (2002, p. 154) identified four negotiating positions: 1) true believers in free trade, such as Alberta, who took a more principled view towards free trade, and Manitoba, which understood its position as

⁴⁵¹ Interview with former senior provincial government official, 17 August 2015.

⁴⁵² Interview with former senior provincial government official, 7 August 2015.

the ‘keystone’ province; 2) the skeptics, including Saskatchewan and BC, who were not convinced of the benefits of the AIT but would sign off eventually to preserve national unity; 3) Ontario, torn between its economic need for a strong agreement and its government’s ideological doubts; and 4) the pragmatists, including the Atlantic Provinces and Québec, who carefully sought mutual recognition as well as liberalization but had their own specific interests to defend. Table 3 summarizes provincial positions on both internal and external free trade, demonstrating that support for free trade did not completely overlap with partisanship. These negotiating positions were reflected in Wilson’s notes preceding the March 1993 CMIT meeting.

Table 3: Provincial Governing Parties and Support for Free Trade, 1993

<u>Territory</u>	<u>Governing Parties circa January 1994</u>	<u>Support for free trade: internal</u>	<u>Support for free trade: external</u>
Alberta	Progressive Conservative	X	X
Manitoba	Progressive Conservative	X	X
BC	NDP		X
Saskatchewan	NDP		X
Ontario	NDP		
Québec	Liberal	X*	X
Nova Scotia	Liberal	X*	X
New Brunswick	Liberal	X*	X
NFLD	Liberal	X*	X
PEI	Liberal	X*	
Canada	Liberal	X	X

X* Conditional support

The political economy also played a key role in generating provincial reluctances towards the AIT. Across the country, provinces were becoming more and more integrated with the American market. Trade between Canada and the USA “is strongest between regions with similar industrial structures, but this trade tends to be limited to regions in close geographic proximity. As the distance between regions increases, trade based on different but complementary industrial structures becomes dominant” (W. M. Brown & Anderson, 1999, p. 24). In other words, trade between provinces and states is first by proximity and intra-industry trade owing to regional specialization, second by inter-industry trade. Indeed, there exists only four very strong bilateral regional relationships based on intra-industry trade – Ontario and the Great Lakes, Mid-Atlantic, and South Atlantic States; Québec and New England; Prairies and Plains; and Alberta, BC, and Rocky Mountain States (ibid., p. 43).⁴⁵³

The dependence of provincial industries on exports and the most exported commodities in each province for 1990 are reported in Table 4. These figures confirm a trade structure that is heavily dependent on international trade, which is overwhelmingly directed towards the USA. Helliwell (1998) confirms this when he finds that the border effect is lowest for the most resource-dependent provincial economies, particularly the three westernmost provinces, i.e., all things being equal, they are more apt to trade with the USA than with other provinces. The border effect is also lower for some manufactured goods, including machinery and equipment, possibly due to the relatively high foreign ownership share of Canadian manufacturing. Indeed, high foreign ownership may only compound the observation that resource- and manufacturing-

⁴⁵³ See Helliwell (1998), who argues international trade is actually national markets linked by threads of foreign trade and investment.

dependent provinces all experience the pull of the American market, reducing over time their dependence on internal trade.

The trade structure of provinces and their reliance on international trade is compounded by the fact that provincial economies are reliant on only a few sectors for the bulk of their trade. After the FTA, Ontario's proximity to the US Northeast and their similar manufacturing-heavy industrial structures produced the most north-south integration. Québec, which relies less on manufacturing but is also proximate to American manufacturing states, experiences the second highest level of integration. Then the West, which is less integrated since its major exports are not necessarily to proximate states, followed by Atlantic Canada, which is furthest from American markets and so integrated the least (W. M. Brown & Anderson, 1999). Provincial economies are anchored to the American market, owing to their dependence on cross-border trade and specialization in a few key sectors. When confronted with internal free trade negotiations, the provinces failed to see the urgency of the issue and therefore resisted amending their powers over the economy, focusing instead on securing market access and on regional development.

Table 4: Provincial Industries' Dependence on Exports, and Commodities Most Exported, 1990

Legend:		Industry sends >60% of output overseas					
		Industry sends >30% of output internally					
		Industry reliant on both internal and external exports					
Industries Most Dependent on Export Markets - 1990					Commodities Most Exported - 1990		
		% of output					
British Columbia		interprovincial	international		% of total international exports		
Mining		3.2	92.2		Lumber, sawmill, wood products	21.8%	
Paper & allied products		8.6	82.9		Paper & paper products	20.5%	
Fishing & trapping		8.8	79.9		Transportation & storage	13.8%	
Logging & forestry		9.4	74.8		Mineral fuels	5.7%	
Primary metal products		20	70.7		Mining products	5.5%	
					Primary metal products	4.8%	
					Fishing & trapping	0.9%	
					Forestry products	0.5%	
					Total provincial international exports: 19,511 (\$ millions)		
		% of output					
Alberta		interprovincial	international		% of total international exports		
Paper & allied products		13.4	74.1		Mineral fuels	44.1%	
Chemicals & chem prod.		32.4	58.3		Chemicals & chemical prod.	9.1%	
Pipeline transport		34.7	56.3		Transportation & storage	8.7%	
Primary textile & textile prod.		31.7	49.4		Agricultural products	7.8%	
Crude petroleum & natural gas		41.7	48.6		Petroleum & coal products	7.4%	
					Paper & paper products	3.1%	
					Textile & clothing products	0.6%	
					Total provincial international exports: 16,692 (\$ millions)		
		% of output					
Saskatchewan		interprovincial	international		% of total international exports		
Mining		12.1	81.6		Agricultural products	33.7%	
Paper & allied products		16.2	77.3		Chemicals & chemical prod.	15.0%	
Storage & warehousing		35.9	57.1		Mineral fuels	14.8%	
Crude petroleum & natural gas		46.1	45.9		Transportation & storage	8.2%	
Pipeline transport		55	33.9		Wholesale trade services	6.4%	
					Mining products	5.8%	
					Paper & paper products	5.1%	
					Petroleum & coal products	0.7%	
					Total provincial international exports: 5,358 (\$ millions)		

		% of output				
Manitoba		interprovincial	international		% of total international exports	
Primary Metal products		26.5	67.5		Agricultural products	18.9%
Mining		30.4	66.4		Primary metal products	17.9%
Storage & warehousing		45.3	46.6		Transportation & storage	14.9%
Crude petroleum & natural gas		57.1	41.1		Machinery & equipment	10.2%
Electrical & electronic products		64.5	24.5		Autos, trucks, other transp. equip.	9.0%
					Mining products	2.2%
					Electrical & communication prod.	0.7%
					Petroleum & coal products	0.0%
				Total provincial international exports: 4,197 (\$ millions)		
		% of output				
Ontario		interprovincial	international		% of total international exports	
Transportation equipment		9.9	81.1		Autos, trucks, other transp. equip.	44.1%
Mining		12.8	72.3		Machinery & equipment	6.3%
Primary metal products		23.9	58.1		Primary metal products	6.2%
Rubber products		28.6	47.5		Electrical & communication prod.	4.0%
Paper & allied products		28	45.2		Paper & paper products	3.7%
					Mining products	2.9%
					Rubber, plastic products	1.5%
				Total provincial international exports: 75,462 (\$ millions)		
		% of output				
Quebec		interprovincial	international		% of total international exports	
Mining		10.6	75.4		Autos, trucks, other transp. equip.	14.3%
Primary metal products		25.2	61.9		Primary metal products	12.8%
Transportation equipment		27.7	57.5		Paper & paper products	12.1%
Paper & allied products		29.3	52.1		Electrical & communication prod.	10.6%
Rubber products		36.4	45.2		Mining products	6.6%
					Rubber, plastic products	1.6%
				Total provincial international exports: 29,725 (\$ millions)		
		% of output				
New Brunswick		interprovincial	international		% of total international exports	
Paper & allied products		13.4	83.6		Paper & paper products	33.1%
Fishing & trapping		18.1	77		Transportation & storage	10.4%
Logging & forestry		16.3	71.7		Food products	9.0%
Mining		26.8	68.4		Mining products	7.8%
Primary metal products		54.1	32.5		Petroleum & coal products	6.7%
					Lumber, sawmill, wood products	5.2%
					Fishing & trapping	2.3%
					Primary metal products	0.9%
				Total provincial international exports: 3,537 (\$ millions)		

		% of output				
Nova Scotia		interprovincial	international		% of total international exports	
Paper & allied products		17.5	77.4		Food products	22.6%
Fishing & trapping		22.8	71.8		Paper & paper products	17.6%
Rubber products		37	56.1		Rubber, plastic products	10.2%
Primary metal products		38.8	51.4		Wholesale trade services	9.8%
Primary textile & products		75.4	13.8		Transportation & storage	7.0%
					Fishing and trapping	2.5%
					Primary metal products	1.4%
					Textile & clothing products	0.8%
					Total provincial international exports: 2,620 (\$ millions)	

Alberta and Manitoba: free traders

According to Minister Wilson's notes, Alberta strongly supported the internal trade initiative and was ready to join the negotiations. The one problem was that Alberta "will only back away if the meeting appears to be producing a cosmetic result without any real commitment from provinces". They, along with the negotiation's other supporters, should be used to "persuade those that are uncertain".⁴⁵⁴ Of all the provinces, Alberta was the most certain, "believing that a more open domestic market will offer increased opportunities for Alberta business and increase our competitiveness".⁴⁵⁵

Between 1971 and 2015, the Progressive Conservative Party governed Alberta. The Party believed in all aspects of free trade as a matter of ideological concern. Alberta supported free international trade early in its history, owing to its resource-producing economy, first in agriculture and then in energy and mining. This did not preclude a role for the government in economic development; Premier Peter Lougheed was a major proponent of establishing forward

⁴⁵⁴ Archives of Ontario, Folder B501234 – Meeting: Chief Negotiators-Task Force of Officials on Internal Trade, "ISTC: Objectives and Scenario notes," March 1993, p.6.

⁴⁵⁵ Alberta FOI request (2015-G-0007): Applicant Package Part 1, "Memo for Asst Deputy Ministers from AB Economic Development and Tourism," 13 July 1993, p.19.

and backward linkages to the energy extraction industry. Moreover, he had “abandoned the strategy of working from within the central government for national economic development, in favour of regional or provincial economic autonomy” (Cooper, 1996, p. 37). Despite the common roots of prairie socialism in Alberta and Saskatchewan, protectionism – domestic or foreign – was not a policy that Alberta sustained into the latter half of the 20th century. Indeed, according to Cooper (ibid., p.12), “the Government of Canada, along with the other eight provincial governments, must either follow Klein’s way or the Saskatchewan route of Premier Roy Romanow”.

Premier Ralph Klein’s way was to implement a reform programme motivated by debt reduction. The reason was spelled out by *The Wall Street Journal* on 12 January 1995: Canada has “become an honorary member of the Third World in the unmanageability of its debt problem” (ibid., p. 23). This was not unlike Keating’s quip that Australia risked becoming a ‘banana republic’ because of its almost perpetual current account and government deficits. Reform was also a demand of voters: “All across the nation Canadians were indicating...that they were discontent with what politicians were doing and saying” (ibid., p. 29).

Upon Klein’s election in June 1992, he noted that “our first task...was to convince Albertans that the situation was critical...Not...a debt and deficit problem, not a debt and deficit situation; we face in this country a debt and deficit crisis” (ibid., p. 29). He believed his job was to “get out there and do some hard-nosed selling” (ibid., p. 99). Only a few years earlier, both Premier Greiner of NSW and PM Hawke were connecting international trade with domestic efficiency and competitiveness and sought a reform programme designed to harness this linkage. Whilst Hawke was founding APEC, Klein was touting Alberta to Asian investors (Lisac, 1995, p.

160). In fact, he flew to Asia days after announcing a 20% spending cut across the board. Rather than see the trip as dodging the ensuing criticism, for Klein the two issues were linked: “[The combination of 20% cuts and low tax rates] was a budget policy apparently written to fit the requirements of what-ever anonymous force had created a megalopolis in the dusty Korean hills [referring to the South Korean capital, Seoul]”. Klein would call this the Alberta Advantage, which in the eyes of many Asian investors also included access to resources (ibid., p. 163). Indeed, energy accounted for 51.5% of Alberta’s international exports in 1990. As well, several Alberta industries were relatively dependent on interprovincial trade, particularly crude petroleum & natural gas, chemicals, and textiles (Statistics Canada, 1996). Alberta’s dependence on energy exports, its recognition that interprovincial trade helped shore up its economic diversification, and the Progressive Conservative Party’s ideology all point to Alberta’s support for both internal and external free trade.

By 1993, Alberta’s deficit topped \$3.4 billion, with approximately 10% of the budget spent on servicing debt (Lisac, 1995, p. 189). As part of its deficit reduction plan, Alberta reduced the government’s share of GDP from 17.3% in 1995 to 12.9% in 1997. It did so by reforming government regulations and activities (such as deregulating milk prices), simplifying royalty reviews, and privatizing public monopolies (such as AB Government Telephones, Treasury Branches, and Liquor Control Board). Klein did not need an AIT to begin reforming Alberta’s barriers to trade. At times, the pace of change meant that “Albertans were getting used to having to wait to figure out what was going on” (ibid., p. 182). With the advent of the AIT, Alberta saw a chance to have its reforms go nationwide.

Cooper (1996) also demonstrates that Alberta's budgets at the time were directed toward economic development, a goal of the PCs since their 1971 election and really the same goal of every other province. However, the Progressive Conservative government's efforts were drastically different than previous attempts. Past governments had tried to pick winners, but in fact "they almost invariably picked...losers...The Klein Government has reduced both individual and corporate welfare dependence" (Cooper, 1996, p. 44). Thus, Alberta perhaps was one of the first Canadian provinces to abandon the policies exemplified by Victoria's Cain government: government trying to pick winners. It replaced its past economic development policies with the Alberta Economic Development Authority, a partnership between experts within government and the private sector who were tasked with encouraging investment, exports, and deregulation and also examining practices that were impeding development and growth. Alberta was also heavily influenced by reforms in New Zealand, which had also influenced reforms in Australia. Alberta's economic development and privatization policies meant it "would be a net beneficiary of a more accessible [internal] market since we have relatively few preferential practices of our own".⁴⁵⁶

Thus, in Canada, Klein played the role of reform cheerleader. Like NSW Premier Greiner, he was an enthusiastic reformer and debt reducer and led a party in opposition to the parties in power federally and in most of the other sub-units. Both leaders believed that regional economic development would be served by national reforms. But despite their enthusiasm, Alberta was no Canadian version of New South Wales. Klein's influence was limited in ways that Griener's was

⁴⁵⁶ Alberta FOI request (2015-G-0007): Applicant Package Part 1, "Alberta Action Plan for Internal Trade Barrier Negotiations," August 1993, p.107.

not: he was considered too-right wing, too polemical, and his budget cuts were too drastic. Instead of encouraging others to join him, Klein's ways were anathema to his provincial counterparts and so, unlike NSW, Alberta did not serve as an example to the other provinces of the benefits of reform.

Manitoba's support for the internal trade negotiations was very much a product of its geography; it is the hub between east and west. A growing Canadian market means more business for the keystone province, with Manitoba being the link between Canada's traditional centre and its growing Western periphery. Manitoba's economy – the most diverse in the country – also meant that it stood to gain no matter what sectors were included in the final agreement. Its regional development would be served by national reforms: several of its industries rely heavily on interprovincial exports and it also exports a more equally weighted diversity of primary, secondary, and tertiary products (Statistics Canada, 1996).

These geographic and economic characteristics place Manitoba in the middle ground of provinces: "Manitoba's economy grows 'steady but slow' in the good times, and 'slow and steady' during the bad...[It is] neither envious of provinces with greater riches nor jealous of those with more political voice" (Hum & Simpson, 2010, p. 303). Its diversity of foreign exports and reliance on internal trade contribute to this dynamic, which led the MB Minister of Industry to convince all AIT parties to select Winnipeg as the location of the ITS, where it is located to this day. Manitoba's position on internal trade "has always been positive, forceful, and unambiguous".⁴⁵⁷

⁴⁵⁷ Alberta FOI request (2015-G-0007): Applicant Package Part 2, "Letter from Minister Downey to Manley," 9 August 1994, p.301.

It also helped of course that Manitoba was governed by the Progressive Conservative Party at the time, which very much shared the economic and political orientation of Alberta, perhaps with less zest and zeal than those ‘cowboys’ on the Rocky Mountain foothills since Manitoba’s political culture is “moderate, medium, diversified” (Dyck, 1996, p. 381; Wesley, 2010). As well, Manitobans have generally preferred a strong national government and its provincial governments “have accepted a policy leadership and program-standard setting role by the national government”. One exception was Premier Gary Filmon, who advocated for more provincial tax room and less federal-provincial overlap in service provision (Thomas, 2010, p. 279). Filmon was also noted as being the first to sign the 1989 Government Procurement Agreement “and intervened on several occasions to resolve impasses and gather support for [it]”.⁴⁵⁸ As will be seen in the Ontario section, Manitoba was not the only province calling for a renewed fiscal federalism but Manitoba’s political economy meant that even without fiscal reform, it supported Ottawa’s reform effort.

Saskatchewan and British Columbia: skeptics

Saskatchewan, BC, and Ontario paint interesting portraits of NDP governments at a time of liberalization, deficit reduction, and de-regulation. Immediately upon entering office in Regina, the NDP sought to stabilize the deficit situation: “many questioned the speed with which the [NDP] leadership moved on the issue” but the government held firm because of the leadership of Premier Roy Romanow (Leeson, 2001, p. 8). Nevertheless, Saskatchewan regarded the AIT as

⁴⁵⁸ Ibid., p.302.

an intrusion into its economic jurisdiction that could detract from its ability to protect its social programs and regional development.

Saskatchewan believed the AIT mattered little to its resource-based, internationally-oriented economy. Agricultural products comprised a third of its international exports; indeed primary goods accounted for 55% of total exports. A further 9% of exports were from chemicals yet, unlike Alberta, Saskatchewan's economic diversification is not tied to interprovincial trade. Its interprovincial trade-dependent industries were crude petroleum & natural gas and pipeline transportation; even storage and warehousing was dependent slightly more on international than interprovincial exports (Statistics Canada, 1996). What good was an internal free trade agreement that could limit Saskatchewan's ability to respond to changes in its primary goods markets? As mentioned above, Alberta and Saskatchewan at the time represented opposite fiscal policy choices. On the one hand, Klein was engaged in massive expenditure reductions whilst Romanow sought to raise taxes in order to balance the budget. One such tax raise was in Crown utility rates "to increase their 'profits'. These are not really profits so much as monopoly rents since it is inconceivable that SaskTel, SaskPower or SaskEnergy could ever fail to make a profit so long as the province is inhabited" (Cooper, 1996, p. 13). Therefore, Saskatchewan's intransigence regarding internal trade was due to its fiscal policy as well as its international position. If Crown corporations were being used to balance the budget, than why would it agree to restrict its control over those same corporations in an internal trade agreement?

Saskatchewan's desire to retain as much policy flexibility as possible is a significant factor in its skepticism toward the AIT. Its position on the issue was determined by its economic structure: its most valuable export sectors relied more on international export. Even though

Alberta had roughly the same economic structure, the difference in policy positions is explained by economic development as well as by partisan and ideological orientations. Saskatchewan was years behind Alberta in terms of economic development and diversification. Catching up required maintaining and growing its exports to the USA and also to Asia, which demanded maximal policy capability. Regional economic development would not be served by national reforms. Alberta supported foreign and internal free trade and believed the market and its Development Authority would foster growth. Saskatchewan was focused on foreign trade and believed government intervention would foster growth.

The counter example is Western Australia. It too relied heavily on the foreign trade of resources yet it eventually joined the SPC process. Diffuse external economic integration – exemplified by the shift in exports toward Asia – produced real risks and thus an incentive to cooperate on domestic reforms, especially in the context of the Commonwealth's reforms to the exchange rate and tariff structure. WA could no longer rely on exports to the West nor could it remain competitive with Asia on its own. The WA Labor government's policy of state interventionism was engulfed in failure and political scandal and Canberra's tariff reforms and financial liberalization were making such policies more and more difficult to sustain. On the other hand, Saskatchewan, emboldened by its NDP allies in BC and Ontario and comfortable with its concentrated market integration with the USA, resisted domestic reforms that would curtail its powers over the economy. Therefore, two left-of-centre parties – NDP and Labor – governing relatively small sub-units reached fundamentally different conclusions on how to approach national economic reforms because of their exposure to different political economic incentives.

Like Saskatchewan, BC's NDP government held the opposite position from Alberta: it was uncertain whether a formal agreement was necessary and had little interest in its eastern neighbours. Wilson's notes indicate that BC's position "will likely be that it is not an important issue for them and there does not appear to be too much concern in their constituency".⁴⁵⁹ In a briefing note prior to the June 1993 CMIT meeting, it was reported that "the BC Cabinet was apparently reluctant to give Minister Zirnhelt a mandate to participate. However, it is unlikely that Ontario will receive much active support from BC or any other province during the meeting".⁴⁶⁰

A letter from then BC Premier Mike Harcourt to PM Chrétien provides further insight into BC's priorities.⁴⁶¹ Dated 11 July 1994, just days before the AIT was signed by First Ministers in Ottawa, Harcourt acknowledged the upcoming internal trade discussions and then raised other issues, including the USA's refusal to abide by the Pacific Salmon Treaty, the softwood lumber problem, and sewage treatment infrastructure. On internal trade issues, Harcourt informed Chrétien that "the realization of BC's full economic potential is much more depending upon such issues as tax and fiscal policy changes..., the future of our transportation system..., and identifying priority federal investments in BC's science and technology sector". A deal on Canadian internal trade "would do less for our economy than a single deal on infrastructure development with one

⁴⁵⁹ Archives of Ontario, Folder B501234 – Meeting: Chief Negotiators-Task Force of Officials on Internal Trade, "ISTC: Objectives and Scenario notes," March 1993, p.6.

⁴⁶⁰ Archives of Ontario, Folder B510234 – CMIT June 7-8/93, "Minister's Briefing Note: CMIT Vancouver," 7-8 June 1993, p.1.

⁴⁶¹ PCO FOI request (A-2014-00381/JL): "Letter from Premier Mike Harcourt to Chrétien," 11 July 1994. The letter was obtained from a FOI request to the Privy Council Office for any correspondence between the PM and any Premier between 1992 and 1995 on the issue of internal trade. After several rounds of talks with the Privy Council Office Director of Access to Information, it was discovered that only this letter matched all the requirements. It is now too late to file further requests to broaden the search. Instead, access requests were sent to Industry Canada for correspondence between Ministers, as well as requests to the Ontario, Québec, and Alberta governments.

of our Pacific Rim trading partners”. Harcourt also believed that the AIT was “not consistent with our need to be able to build a strong economy and ensure that British Columbia’s citizens benefit from the spending of their tax dollars”. In closing, Harcourt acknowledged that “compromise is a necessary feature of viable federal-provincial relations”.⁴⁶²

In other words, BC will participate but the AIT really does not benefit the province and in fact curtails the provincial government’s ability to support local industry. No wonder Manley’s Cabinet memorandum acknowledged that BC has “little incentive...to limit its policy options and instruments”.⁴⁶³ As well, BC voiced its belief that fiscal issues were more of a priority than domestic economic reform. Indeed, at the 1991 Annual Premiers’ Conference, then BC Premier Rita Johnson stated “we are not...prepared to have Ottawa unilaterally renege on cost-sharing agreements that we signed in good faith...[T]here has to be more cooperation and coordination between federal and provincial governments on such matters”.⁴⁶⁴ There is every possibility that with an honest inducement, such as offering reform to fiscal federalism, Ottawa could have engaged BC proactively rather than see it sit on the sidelines.

The focus on issues other than internal trade is not surprising considering Harcourt’s view of the March 1992 FMM on the Economy. He recalled that his fellow NDP Premiers, Rae and Romanow, launched a heated attack on the Mulroney government’s downloading of costs to the provinces even as they were all supposed to agree on an action plan for the economy: “There went any hope of consensus on economic problems. It was every province for itself. In the future,

⁴⁶² Ibid.

⁴⁶³ PCO FOI request (A-2014-00381/JL): Doc. 3-0002-94MC(01), 24 December 1993, “Memorandum to Cabinet: Intergovernmental Negotiations on Internal Trade,” p.19.

⁴⁶⁴ Ottawa, “32nd Annual Premiers’ Conference, documents: Opening Remarks by Premier Rita Johnston, BC,” 26-27 August 1991, p.3.

I said to myself at the time, I would rely less on trying to play 'Captain Canada' and more on furthering BC's interests" (Harcourt & Skene, 1996, pp. 80-81). Harcourt's view reflects the typical mood of Victoria-Ottawa relations, which "have long been characterized by misunderstanding and bemusement, by suspicion and anger and, worst of all, by periods of mutual indifference and detachment" (Black, 1996, p. 32). At times, the suspicion and mistrust emanate from federal and provincial differences over the relationship with the USA, as indicated by Harcourt's letter to Chrétien. BC's relations with the rest of Canada have been further stressed since "global economic change has renewed the sense of a Pacific distinctiveness" (ibid., p. 43). Québec is not the only province to seek recognition of its uniqueness, although Resnick (2000) notes there is a difference between uniqueness based on region (BC) versus nation (QC).⁴⁶⁵

The result was BC felt that, like Saskatchewan, it could go it alone on domestic economic policy. A similarly Asian-focused sub-unit, Western Australia, is also an interesting comparator for BC. Both were focused on Asian trade yet WA was induced to join a national reform programme whilst BC was not. The difference is not only the more narrow reform program offered by Ottawa but also BC's more concentrated market integration with its immediate neighbours, the Americans and Pacific Rim. BC, like WA, is unique among the provinces for relying heavily on exports from one industry, forestry, and has no major industry reliant on interprovincial trade. Forty percent of BC's exports were in paper and woods products, and every one of its primary goods industries overwhelming sent their output overseas (Statistics Canada, 1996). WA's trade too diffuse to offer it the protection that is characteristic of BC's trade

⁴⁶⁵ Resnick (2000) also questions whether Courchene overreached in his analysis of Ontario as a North American region/nation state.

structure. In the future, as WA trade relies increasingly on China, a reversal of its incentive to cooperate may be in store (this is more fully explored in the conclusion).

BC also felt it could go it alone because its deficit situation was not as dire as the other provinces. In the 1990s, BC's government faced a sluggish economy and a budget deficit: "For many of the NDP's traditional supporters, one of the more distressing developments since the party came to power was its gradual shift toward fiscally conservative economics" (Gawthrop, 1996, p. 235). Even before the 1991 election, the NDP was preparing a policy of balancing the budget "over the business cycle", a policy it shied away from upon entering office. There was much disagreement within the Party, with some responding that the proposed 15% cut to all ministries was unnecessary since over the long-term, even a deficit increase to cope with the recession would not impair BC's credit rating. In contrast to Alberta's cuts, BC avoided a scorched-earth, slash-and-burn policy. Rather, BC had "the fiscal flexibility to maintain basic services, to maintain a positive role for government in a mixed economy" (ibid., p. 238). Thus, while Alberta abandoned direct government intervention, BC sought to sustain it.

As well as dealing with the deficit, Harcourt was crafting a long-term economic development plan. Several roundtables and summits were held between 1992 and 1995. The plan contained four priority areas: long-term job creation and economic growth, skill development, forest sector renewal, and fiscal management. "The tone...is one of pragmatism. The NDP recognized the global trend toward deregulation and free trade". The plan rejected the deficit-fighting ethos of Alberta and instead "encouraged the government to invest in skills training programs, quality infrastructure and the strength of BC's natural resources base" (ibid., p. 254). According to Harcourt, "BC represented, in my mind, the future direction of this country,

with its huge growth potential associated with the Pacific Rim” (Harcourt & Skene, 1996, p. 82). Such growth potential fit well with BC’s “tendency toward specialization in production for external markets. Much of this trade has always been...resource related” (Howlett & Brownsey, 1996, p. 24). In other words, BC had no incentive to voluntarily constrain its economic policy-making via an internal trade agreement or cooperative federalism. As well, refusing to agree with Ottawa’s plan had no direct consequences so long as fiscal reform was off the table.

The results of its policies were clear: “By 1995,...BC had the most vibrant economy in Canada, the lowest unemployment rate (9.1%), the highest growth rate (4.6%), the highest number of jobs created (50,000 new jobs in 1994), and the strongest credit rating” (Gawthrop, 1996, p. 256). Simply put, there was little risk in resisting an internal trade deal: “[BC] had a huge role to play in Canada’s economic future and we wanted the freedom to make that mark, unhindered by old-fashioned, centralist Canadian thinking” (Harcourt & Skene, 1996, p. 84). With its trade concentrated on the USA and Asia, and with reform to fiscal federalism off the table, BC’s economic structure and the negotiations themselves provided little incentive for intergovernmental cooperation on economic or institutional reforms that could risk limiting its ability to exercise its full sovereign powers over the economy.

Atlantic Canada and Québec: pragmatists

According to Wilson’s notes, “in general Newfoundland, Nova Scotia, New Brunswick, Manitoba and Alberta will support the negotiating process”. The Atlantic Provinces were concerned primarily with regional development; any agreement hamstringing their ability and that of Ottawa to invest in the region were unacceptable. Naturally, they wanted an exemption for regional policy. According to Dan White, past president of the Industrial Cape Board of Trade,

when the CMIT negotiations were hosted in Halifax, the business community showed a lack of interest because “Atlantic Canada is struggling with so many difficult and challenging issues right now, from the fisheries to decline in the pulp and paper industry”.⁴⁶⁶ Nova Scotia’s major exports were tied to primary goods, with food products and paper products comprising 40% of its international exports. Paper and fishing were two industries that sent three-fourths of their exports overseas. Its interprovincial trade-dependent industries were all in manufacturing. Thus, for Nova Scotia, internal free trade was important but not at the cost of the province’s regional development. Its negotiators would not prevent an agreement outright but they were determined to ensure their specific needs were met.

New Brunswick presents an interesting case, demonstrating the importance of regional development. In terms of its economy, NB resembles BC: it relies heavily on forestry exports (approximately 40%) and almost all of its primary industries send the overwhelming majority of their output to the USA. Yet rather than refuse to participate in the AIT, and ally with BC and Saskatchewan in the skeptics category, New Brunswick remained a pragmatist. This is partially due to its Liberal government, who did not reject free trade outright like the NDP. But as this dissertation has sought to demonstrate, partisanship is not the only explanation. New Brunswick’s historical reliance on regional development, plus its midway position between the Atlantic and Eastern markets and its historical and political bonds with the other Atlantic Provinces, conditioned its government to support the AIT.

In Atlantic Canada, the political economy played a role in conditioning the choice of whether or not to support a domestic reform programme. Regional economic development

⁴⁶⁶ Québec Archives, Box 24 A 001 09-04-003B-01, File 2005-10-003\271, “Ottawa CBC interview,” 6 Apr 1994, p.2.

would not be achieved in any meaningful sense by national reform, which Atlantic Canadians know intimately. Nova Scotia and New Brunswick's primary industries rely on international exports. In this regard they share characteristics with BC and Saskatchewan: their major economic sectors are resource-based and are focused on overseas markets. When coupled with regional development and their reliance on Ottawa, the Atlantic provinces lukewarmly supported the AIT.

Regarding Québec, Wilson's notes state that "[its] position is uncertain" and major disagreements between Ontario and Québec were still outstanding: "The only way to prevent this from becoming an issue is to persuade Quebec that comprehensive negotiations are more important to them than wine". Québec and Ontario "will be critical. The strategy for them is to try to resolve any outstanding issues between them or, at least, agree to proceed with the negotiations and leave some issues until later".⁴⁶⁷ Resolving their mutual disagreements was important because Québec and Ontario, despite having different political economies (Québec being more statist and collaborative whilst Ontario is more liberal and market-oriented), were similarly affected by globalization and international liberalization (Haddow, 2015). Meeting these challenges required some cooperation.

The existence of a significant and localized linguistic minority as well as the partisan political issue of Québec nationalism is usually the factor that distinguishes Canada from other most-similar cases. However, the following analysis reveals that the political economy is an

⁴⁶⁷ Archives of Ontario, Folder B501234 – Meeting: Chief Negotiators-Task Force of Officials on Internal Trade, "ISTC: Objectives and Scenario notes," March 1993, p.6.

important yet overlooked factor that conditioned behaviour towards internal trade reform. What was unique was that Québec was the only province to face the electoral gun in 1994, which helped spur attempts to reach an agreement by the June deadline. This was Chrétien's tactic in the lead up to the 1995 sovereignty referendum: "[Chrétien] still held to the complacent notion that the best strategy was good government. 'Some say I have no plan to resolve the problems,' he said... 'If we provide a good, honest, solid working government, everybody will want to remain in Canada'" (L. Martin, 2003, p. 115).

For the provincial Liberal government, showing that federalism worked as well as opening the economy were complementary goals. Quebec City wanted broad objectives, a minimalist dispute resolution process, and regional policy exemptions. Yet according to the Manley memorandum, Québec "is reluctant to take the lead on any issue".⁴⁶⁸ Some have argued this gave Québec a strong negotiating position, whereas the Québec negotiators themselves felt they were under pressure to secure a deal at any cost. "A more measured perspective may be that Quebec was a constructive if tough negotiator, strongly in favour of the basic objectives of the AIT but sensitive in certain areas" (D. Brown, 2002, p. 159). The sensitivities were held at the bureaucratic level and were eventually circumvented by directly appealing to the Premier, who wanted a successful deal. Indeed, the *Toronto Star* reported two days after the deal was signed that the AIT "was seen as a gift to Premier Daniel Johnson in the days before an election campaign" (Toronto Star, 1994b).

⁴⁶⁸ PCO FOI request (A-2014-00381/JL): Doc. 3-0002-94MC(01), 24 December 1993, "Memorandum to Cabinet: Intergovernmental Negotiations on Internal Trade," p.19.

Along with Alberta, Québec has been a strong supporter of the FTA (J. H. Thompson & Randall, 2002, pp. 286, 291). Such support is found within both of Québec's governing parties (Haddow, 2015). Québec has also been a strong defender of provincial rights, particularly in its pursuit of 'profitable federalism'.⁴⁶⁹ This combination placed Québec in the pragmatist category (D. Brown, 2002). It reached this position in the 1980s, when free trade was on the national agenda and the national question overtook economic issues as the dominant cleavage in Québec politics.⁴⁷⁰

However, Québec's support for openness is conditioned by heavy state intervention in economic development. As a result of the Quiet Revolution, Quebec City began to actively encourage indigenous enterprises, resembling a French model of *dirigisme*, which has dissipated over time with the emergence of a healthy French-speaking business class. Upon coming into power in December 1985, Bourassa's Liberal government began the process of 'normalizing' the Québec state and economy. The Liberals had firmer links with Francophone business leaders than the Parti Québécois – many of whom were in the Liberal caucus and cabinet – and consulted with them widely on potential changes. These included working more effectively within the IGR system, privatization, and reducing government intervention. The results, according to McRoberts (1999), were mixed due to the reaction from groups not consulted, especially labour unions. Yet Bourassa did manage to privatize many state-owned enterprises, such as Québecair and Domtar Inc., and proceeded to adopt at least the rhetoric of neo-liberalism.

⁴⁶⁹ For an overview, see Alain-G. Gagnon and Garcea (1988).

⁴⁷⁰ See Bélanger and Nadeau (2009).

By the time Daniel Johnson Jr. became Premier, the government was focused on bringing the economy through the 1990 recession, starting with a “frugal” cabinet (Gignac, 2007, p. 253). One major plank of his agenda was to focus on several cluster industries that were based in Québec and internationally competitive. The policy was partly a carryover from when Johnson was Minister of Industry and Commerce in Bourassa’s cabinet. The program’s results were mixed yet its implementation showcased that Quebec City was more willing than Toronto to intervene in the economy through direct negotiations with business and labour or through its Crown corporations. In fact, Bourassa’s normalization process had the effect of expanding the maneuverability of provincial Crown corporations to intervene in the economy, which has the added bonus of helping Québec elude the reach of the federal government (Bernier & Garon, 2004). Internal trade was folded into this strategy of ‘normalization’ (Haddow, 2015) and factored into Johnson’s desire to smooth intergovernmental relations: “Si l’on pouvait, dans ce pays qu’est le Canada, éliminer les dédoublements, s’entendre sur le pouvoir fédéral de dépenser, on bénéficierait de marges de manoeuvre, d’un gain réel quant aux dépenses publiques, et le pays et les provinces ne s’en porteraient que mieux” (Gignac, 2007, p. 255).

Tremblay and Gagnon conclude that Québec’s position on provincial autonomy and jurisdiction was “not going to become outdated or obsolete with the passage of time, globalization or the increasing interdependence of peoples and governments” (Quoted in J. Smith, 2002, p. 55). Hence Québec was seen as a pragmatist. It favoured free trade, but not above its ability to intervene. It wanted a more efficient internal market with no new constitutional constraints at the same time as it supported the FTA and NAFTA. Its goal was to diversify its export base away from the rest of Canada and support its USA export industries, which are

concentrated in three key sectors: pulp and paper, metals and minerals (especially aluminum), and transport materials (particularly auto parts) (Rocher, 2004). In terms of exports, mining, metal products, transportation equipment, and paper products all rely heavily on international export (Statistics Canada, 1996). Its diversified export base resembles Manitoba's yet Québec never championed free trade like its Western cousins. Québec's history of state intervention and its increasing reliance on trade with the United States impacted its desire to cooperate, turning it into a pragmatist that was a ready negotiating partner but determined to argue for as much freedom to manoeuvre as possible. Upon taking office in September 1994, the Parti Québécois signalled it was willing to continue negotiating on specific issues. Premier Jacques Parizeau's government was ready to have an active presence on shared constitutional jurisdictions; everything else would be judged on a case-by-case basis. The Parti Québécois also stated it would actively participate on issues related to opening up markets and the continentalization of certain activities.⁴⁷¹

Since the goal of the AIT was a more competitive domestic economy that could better take advantage of a changing world market, it seems strange that Québec, a supporter of free trade, would not be a full ally of Alberta and Manitoba. A complete explanation must include its political economy: Québec's *modus operandi* of state intervention coupled with its stronger integration with American markets incentivized policy independence rather than cooperation.

Québec represented a model Rae's government may eventually have pursued if it had maintained electoral support. Ontario's skepticism towards the internal trade negotiations

⁴⁷¹ BAnQ Montréal, Z2-830-521/009, "Conference on the Council of Ministers Responsible for Transportation and Highway Safety," 5 October 1994.

mirrors Québec's pragmatism: Québec already intervenes and therefore sought to maintain it to some degree whilst Ontario's NDP sought to build such a policy capacity and therefore actively resisted any constraints on its ability to do so.

Ontario: heartland under pressure

Wilson's notes state that "Ontario has indicated that they are prepared to participate on the comprehensive negotiation...[although they] may propose conditions or ask that some issues be excluded".⁴⁷² On the surface, this analysis seems to match that of Québec. However, the ideological orientation of the NDP meant that instead of remaining a pragmatist or skeptic, Ontario actively tried to put the brakes on liberalization by pursuing exemptions to the AIT's general rules.

In a letter dated 26 June 1992, PM Brian Mulroney implored Premier Rae to "ensure adequate resources are directed forthwith to the task at hand and that Ministers responsible for Internal Trade have authority to speak on their behalf". Mulroney continued, "I would ask that, where appropriate, you reinforce within your government the direction we gave to the CMIT".⁴⁷³ Mulroney's request went unheard for the most part. By the time of Manley's memorandum to Cabinet, Ontario's position during the negotiations was described as "unhelpful" and indicative of the "tough regional and protectionist stance that the Government of Ontario seems to have taken in recent months".⁴⁷⁴

⁴⁷² Archives of Ontario, Folder B501234 – Meeting: Chief Negotiators-Task Force of Officials on Internal Trade, "ISTC: Objectives and Scenario notes," March 1993, p.5.

⁴⁷³ Archives of Ontario, Folder B501234 – Meeting: Chief Negotiators-Task Force of Officials on Internal Trade, "Letter from Mulroney to Rae", 26 June 1992, p.2.

⁴⁷⁴ PCO FOI request (A-2014-00381/JL): Doc. 3-0002-94MC(01), 24 December 1993, "Memorandum to Cabinet: Intergovernmental Negotiations on Internal Trade," p.19.

In the end, getting all parties to agree on comprehensive negotiations was difficult owing to Ontario's position. Ontario officials were briefed on the comprehensiveness discussions in an email dated 18 December 1992 from Deputy Minister Judith Wright: "there appeared to be a general feeling of the inevitability of the process among the other provinces. Everyone concedes that this is election material and if a province doesn't sit down to negotiate it will be singled out as obstructing the elimination of trade barriers".⁴⁷⁵ Ontario's recommendation to better define "what constituted a trade barrier to guide cabinet" was dismissed by Bob Knox. Knox wanted to move directly to the sector negotiations and let the general principles emerge from them whilst Wright wanted the principles to be operationalized immediately for explanation to Cabinet.

Why did Ontario proceed with an internal trade agreement that would help business yet remain intransigent regarding its comprehensiveness? The answer is because Ontario was confronted by conflicting goals. On the one hand, its support in principle for a deal can be traced to its internal trade surplus, international position, and desire to accommodate Québec.

According to Rae, Ontario's reliance on resource exports rather than value-added products "lacks focus and direction" (Rae, 1992, p. 3). Ontario was staring into a future where reliance on the American market was increasingly seen as a liability, but one that few knew how to change: "since WWII, the benefits stemming from the proximity with American markets were such that the province's economic relationship with the world was seamlessly connected to its economic relationship with the United States" (Roy, 2013, p. 145). The new NDP government "went much further than its predecessors in promoting intervention and business-labour

⁴⁷⁵ Archives of Ontario, Folder B501234 – Meeting: Chief Negotiators-Task Force of Officials on Internal Trade, "Email from Wright to McGuire: The comprehensive process begins," 18 December 1992, p.1.

cooperation” (Haddow, 2015, p. 185). With the NDP’s Sector Partnership Fund, industries were encouraged to develop sector-wide plans for government assistance. Sectors without organizations were given government assistance to develop their capacity for strategic planning (Hall, 1998). This policy helped the government avoid the criticism it was ‘picking winners’. When it came to trade policy, the government’s assistance was promised if its presence was helpful in winning foreign contracts. Rae even travelled Europe to deliver the message that Ontario was open for business in the hope of diversifying Ontario’s foreign trade partners. Given Ottawa’s abandonment of industrial policy and the decentralization of federal regional policies, the NDP was confident that the “government’s economic development objectives could be achieved within the context of existing trade agreements” (ibid., p. 66). Improving the internal market for Ontario business was just another policy in its tool kit – and not the most important one – to deal with larger economic problems.

The reality was Ontario could no longer count on a protected Canadian market to purchase its goods. Free trade at home and abroad needed to be addressed: “There will always be a cheaper workforce...We can only achieve competitive advantage when we recognize that it is the skills of our people, the efficiency of regulations, the quality of our public services, and the drive and entrepreneurialism of all our institutions...that we can and will attract new activity in the economy” (Rae, 1992, p. 7). Courchene and Telmer (1998) argue that Ontario’s manufacturing industry avoided a major restructuring in the 1970s and 1980s because of its close ties to the American market and the lower value of the Canadian dollar. By the 1990s, the restructuring was in full swing. The process was made all the more precarious because Ontario’s exports are concentrated in one sector, autos and auto parts (representing 44% of international

exports). Its transportation equipment industry is also its most heavily exported commodity. Ontario and Québec both rely significantly on manufacturing exports (80% and 74% respectively). But Ontario and Québec also have significant differences since Québec exports autos and auto parts on a more reasonably balanced scale with other manufacturing and primary goods; Ontario relies even less than Québec on primary goods exports (Statistics Canada, 1996).

The AIT was one of many policies attempting to deal with the economic realities confronting Ontario, particularly the orientation and composition of its trade and the cost structure of its businesses. The AIT would not prevent Ontario's transition to a region state connected to Michigan and New York on the basis of auto manufacturing but it could help to preserve the benefits of its role as Canada's heartland (Courchene & Telmer, 1998).

On the other hand, there was opposition from the trade unions and the NDP's base, not to mention the recession and its budgetary position. These situations meant that Rae was never the 'point man' on industrial policy, indicating that it and the AIT were secondary priorities for the NDP (Hall, 1998). The root of the problem was a period of party system transformation. During this transition, the Progressive Conservatives abandoned interventionist policies and adopted more market-oriented policies.⁴⁷⁶ The result was a more polarized political spectrum on economic-distributive issues by the time of Rae's election (Haddow, 2015, p. 49). The NDP's position on trade was in opposition to the "conventional view" that interventionist policies were "bad [and so] we have to revolutionize government, take government completely out of the field of the economy and let the economy do its thing," which according to Rae is ridiculous: "the idea that the economy itself makes politics irrelevant or meaningless or unhelpful to the human

⁴⁷⁶ Although the intervention was nothing like in Québec during this time. See Haddow (2015).

condition is nonsense" (Rae, 1997 (2001), p. 21). Rae's view was "progressively offside with the prevailing economic orthodoxy" (Courchene & Telmer, 1998, p. 162), including free trade, liberalization, and smaller government. All the Australian states eventually adopted this view, which was not the case in Canada.

Fiscally, Ontario was entering a protracted recession and era of cost-cutting. Downloading from Ottawa would cost Ontario \$10.5 billion between 1991 and 1993: "No other provinces has been affected as seriously by this collapse of fiscal federalism as Ontario...We shall have to re-negotiate the very financial basis of Canada...because we need to deal with the changes in our economy" (Rae, 1992, p. 4). To that effort, the Ontario government commissioned a series of reports highlighting Ontario's place in Canadian fiscal federalism. "Informetrica found that in 1991...the amount by which federal taxes paid by Ontarians exceeded federal government spending in Ontario was \$15 billion...[and] over the past decade, the federal government has been shifting its debt onto Ontario taxpayers".⁴⁷⁷ In sum, Rae stated, "Ontario supports the equalization program, but beyond this, Ontario must receive its fair share, and Ontarians must not be treated differently than people in other provinces. The systematic discrimination against Ontario must stop" (quoted in Courchene & Telmer, 1998). Keeping fiscal federalism off the table gave the NDP another reason to oppose Ottawa's reform agenda.

Since fiscal reform was off the table under both Mulroney and Chrétien, Rae's first budget posted a \$9.7 billion deficit for 1991, most of which was structural owing to the recession. It was decided that Keynesian policies would be used to combat unemployment since the recession

⁴⁷⁷ Archives of Ontario, Folder B399127 – Premier's Council on Economic Renewal #2, "News Release, Office of the Premier," 8 November 1993, p.1.

would be short-lived and Ontario had relatively less debt than other jurisdictions. “The result was the worst of all worlds – a budget Keynesian enough to anger business but not stimulative enough to do much good” (Walkom, 1994, p. 103). Rae’s government never really recovered from its 1991 budget (see Courchene & Telmer, 1998). According to Monahan (1995, p. 238), “it took the Rae government almost three years to learn [the] lesson” that debt and deficits matter.

Having tried Keynesianism, “two-thirds of the way through his term, Rae determined the worst of the recession was over and now it was time to get the books back in shape. That made people even more furious” (Paikin, 2013, p. 93). Part of the catalyst for the turn was projections of a \$17 billion deficit. The plight of New Zealand in the 1980s also made the NDP wary of continuing to spend: “Ministers such as Frances Lankin who had been resistant to massive cut-backs were now convinced the province was just a few months away from hitting a debt wall” (Walkom, 1994, p. 120).

To cut the deficit, Rae attempted to negotiate with the unions to save 40,000 jobs by having them take unpaid days off – the so-called ‘Rae days’. With 65% of the provincial budget composed of salaries, this was one way to continue government investment and find \$2 billion in savings. Rae said, “I didn’t want to take it out of infrastructure, I didn’t want to take it out of capital, because I thought...we would end up slowing down other things that we needed to do” (Paikin, 2013, p. 138). In the early 1980s, when Rae was in the federal Parliament, he championed the cause of fighting unemployment rather than fighting the debt or inflation. Going after the latter worsened unemployment, a refrain he continued as Ontario NDP Leader (Walkom, 1994). According to Rae, he achieved success when negotiating with private business,⁴⁷⁸ but with the

⁴⁷⁸ Jacek (1990) notes the power of Ontario interest groups.

public sector “the assumptions is, well, the government is always going to have money...I think it is hard to get public sector workers to agree to make concessions” (quoted in Paikin, 2013, p. 139).

Whereas Hawke succeeded in getting the union leaders and employers onside, Rae failed to convince everyone to accept his Social Contract program for saving public sector jobs whilst cutting spending and increasing taxes – all part of his ‘three-legged stool’ economic policy. Unpaid days off were legislated by the Rae government rather than negotiated, which almost destroyed the ties between NDP and labour (Monahan, 1995).

Further complicating the situation was the fundamental misunderstanding between the NDP and the provincial bureaucracy. The NDP saw it as slow moving and loaded with obstructionist ‘fat cats’ even though several senior aides have since stated they were ready to make changes. Many in the NDP had never worked in government and misunderstood its procedures and institutional culture. In turn, the civil service was not accustomed to the NDP’s consensual style of decision-making, to the point that in Cabinet the Premier sometimes did not have the final say on policy (Walkom, 1994; R. White, 1998). The effect was a listless government seeking reforms via a skeptical civil service. It did not help that “Ontario’s political culture puts a premium on first ministers who are solid, competent managers rather than visionary leaders” (Loreto & White, 1990, p. 80). The NDP in Ontario lasted only one term in power. Upon entering office in 1995, Progressive Conservative Premier Mike Harris undertook massive spending cuts in order to reduce the deficit (Eves, 1995; Harris, 1995).

All these elements combined to place Ontario in the position that “it saw any deal reached [on internal trade] as an evolving political agreement” (Doern & MacDonald, 1999, p.

67). The AIT's value was merely its contribution to the government's other objectives, which included economic diversification based on a strategy of state intervention. Such ambivalence toward the AIT was very much a product of the NDP's difficult position and Ontario's traditional place in Confederation: it has "rarely been opposed to basic national economic policies" (Dyck, 1988, p. 339) and wants the "'preservation and smooth running' [of Canada]" (Courchene & Telmer, 1998, p. 153). Bob Rae described Canada as a place of different solitudes that requires many ways of bringing people together: "The solutions to our common economic and political problems will come much more easily when we have a clear sense of what we want to do together as a country, a sense of common project" (Rae, 1992, p. 1). Unfortunately, the AIT was not that common project. Perhaps a broader reform programme could have transformed it into one, which could overcome the incentive to compete and retain maximal policy independence.

In sum, the provinces were concerned about their own particular issues and did not trust each other or Ottawa to solve their problems. The AIT was merely a simple agreement to remove some technical nuisances to internal trade; they refused to turn it into an agreement on how they should use their sovereign powers to govern the economy (Doern & MacDonald, 1999). Unlike the constitutional negotiations, the AIT was not a battleground between normative positions on provincial rights and constitutional jurisdictions. Rather it was the means by which each jurisdiction could exercise its authority to achieve some reform whilst ensuring economic development (D. Brown, 2002, p. 152). Peter Morton of the *National Post* described the provinces' position:

[The Parties] all agreed essentially, that the trade barriers should come down. They came out with some noble principles...And now we've reached the

point where Mr. Morrow [sic] has come up with a number of ideas how to do this, and the provincial governments are finding that in fact, they have to make significant changes to way [sic] they do things. And that is causing a lot of problems and they're reluctant to make many of those changes.⁴⁷⁹

The remainder of the chapter demonstrates that provincial political economic incentives directly impacted the AIT as evidenced by the arguments they put forward during the negotiations, which centred mostly on regional development. Overall, provinces' reliance on trade with the USA constrained their policy options and kept them focused solely on their own regional development rather than that of the country as a whole. Regional economic development would be achieved via provincial efforts to increase exports, encourage diversification, and improve competitiveness. Doing so required provincial policy flexibility, which – when used without coordination – produces internal trade barriers. Provincial actors were keen to protect their competitive export industries from internal competition as well as support their lesser industries in the name of regional development and economic diversification. Any gains reaped by provincial industries must be kept within provincial boundaries; improved access to provincial markets by provincial competitors was politically unacceptable. With free trade to their largest trading partner secured, the risk of refusing to reform was low. The political economy incentive to compete and retain policy independence far outweighed the incentive to cooperate to achieve domestic economic reform.

This is a fundamental difference with the Australian case. Down Under, the states recognized the national goal of a more competitive and efficient economic union and its ability to further their own individual economic goals. They could no longer rely on concentrated

⁴⁷⁹ Québec Archives, Box 24 A 001 09-04-003B-01, File 2005-10-003\271, "Ottawa CBC interview," 6 Apr 1994, p.1.

external market integration to secure and maintain their prosperity, which rendered each state's independent management its own economy obsolete. Taking the risk of cooperating with each other and Canberra was induced by the risk inherent in the 'turn to Asia'. The shift, the economic crisis, and Hawke's offer of fiscal reform convinced the states to abandon their overtly competitive behaviour and cooperate for mutual gain. Eventually such an enormous reform effort required IGR institutional change.

It is clear that actors in Canada, with few exceptions, did not come to the same conclusion. The provinces were more risk adverse to federal decision-making and its potential to curtail their ability to intervene in the name of regional development. Free trade with the USA extended and deepened an already existing relationship and provided a strong safety net; there was no shift to manage and therefore no risk to mitigate by changing the domestic economy or the way it is governed. One exception was Alberta, whose support for the AIT starkly contrasts with the reluctance shown by BC and Saskatchewan despite their similar economic structures. For Alberta, the political economy incentive to cautiously approach free internal trade was conditioned by political partisanship and its government's neo-liberal stance on regional development policy, both of which favoured the market. For the others, their regional development concerns severely impacted the mechanism of continuous negotiation above and beyond the partisanship variable. Together, partisanship and political economy tell the complete story of the AIT and its inability to impact IGR institutions.

A lack of reform to fiscal federalism must also be included. The Australian case demonstrates the value of engaging in as broad a reform programme as possible. The Commonwealth may have continued to loom over the states during the SPC process – there was

no neutral chair – but its offer to examine fiscal federalism whilst pursuing economic reform to manage the ‘turn to Asia’ was substantial and genuine enough – because of Hawke’s leadership – to win over the states and bring them to the table as symbolic equals. Canberra’s policy priorities were on the table equally with the states’.

In Canada, the fiscal issue was equally of concern to provincial actors, particularly as the recession played havoc with provincial capacities to finance social programmes. Including fiscal issues in the negotiations may have overcome partisan views on free trade as well as the incentive to compete that is responsible for provincial economic parochialism. Crafting a package deal is the hallmark of the mechanism of continuous negotiation. However, Ottawa was not convinced the issues needed linking. Therefore, when it began organizing the AIT negotiations, the incentive to compete impacted the negotiation structure to create a decentralized process with no whole-of-government approach that lacked the engagement of HoG. The mandate to begin negotiations, which HoG agreed to at their FMM, is therefore construed as a ‘lowest common denominator policy’: something everyone could agree to but difficult to negotiate and implement. Those difficulties prevented the mechanism from functioning as it did in Australia.

Also remarkable was the fact that the provincial positions were mostly at odds with the majority of provincial voters. Federal polling data from the summer of 1992 recorded that “overall, there is widespread support by Canadians for the concept of free trade within Canada”. Ontario and BC residents “are most likely to think their provincial economy would benefit.” And yet these two governments did the most to thwart or stall the entire process! “Residents of Quebec, PEI and Newfoundland are least likely to have a positive outlook in terms of how their

provinces would fare".⁴⁸⁰ And yet again these government were at odds with their voters. Only the reluctance of the two Maritime governments parallels the views of its voters, who were also more likely to perceive the removal of barriers as inflicting job losses on their less developed economies. When businesses were polled, an overwhelming majority favoured removing barriers, with 87% indicating that the provincial governments were to blame and 59% thinking the major obstacle was a lack of commitment by governments.⁴⁸¹

The Agreement on Internal Trade

The last section process traces how the negotiations proceeded, how they were impacted by actors' behaviours, and the reasons for their actions. It demonstrates that provincial skepticism eventually curtailed the mechanism of continuous negotiations and thwarted the effort to complete a comprehensive deal and institutionalize its decision-making process. The extraordinary complexity of Canadian economics and politics managed to achieve only marginal and incremental change.

Nevertheless, when the negotiations began, the major Canadian actors had bought into the AIT process. Ontario officials wanted it

emphasized we supported the objective of freer interprovincial trade...Assuming we got approval to negotiate, we would prepare a list of demands and assumed that all the other province would. The process of negotiation would involve each government coming to the table with a list of what it wanted and what it was prepared to pay.⁴⁸²

⁴⁸⁰ PCO FOI request (A-2014-00381/JL): Doc. 1-0038-93MC(01), 18 February 1993, "Memorandum to Cabinet: Negotiations on Interprovincial Trade," p.39.

⁴⁸¹ Ibid. These figures were repeated in the Manley memorandum (PCO FOI request (A-2014-00381/JL): Doc. 3-0002-94MC(01), 24 December 1993, "Memorandum to Cabinet," p.37).

⁴⁸² Archives of Ontario, Folder B501234 – Meeting: Chief Negotiators-Task Force of Officials on Internal Trade, "Email from Wright to McGuire: The comprehensive process begins," 18 December 1992, p.3.

The federal Cabinet issued instructions to “keep a relatively low profile until the end of the process in June [1994]”.⁴⁸³ The low profile and technical nature of the negotiations limited the role of HoG during the process even though they provided the initial impetus to begin negotiations.

The primary question for the January 1994 CMIT meeting was what kind of agreement the parties wanted to complete: rules-based or sector-based. Lankin’s notes insisted that Ontario must

indicate our view that the negotiations have become too focused on trade irritants and on developing complex and detailed rules to regulate internal trade in Canada. Any internal trade rules...must be simple to understand, useful to business and labour, and, easy to administer. The rules have to balance the objective of a more open internal market with the need for governments to act within their areas of responsibility.⁴⁸⁴

Thus for Ontario, a rules-based agreement was undesirable. Minister Lankin was advised she should ask Federal Industry Minister Manley the following question at the Ministers’ dinner: “given the expressed desire of the new government for more harmonious federal-provincial relations, it is logical to assume that the federal government would want an agreement which promotes the economic union rather than one which fosters disputes amongst the provinces[?]”.⁴⁸⁵ Yet there is a disconnect here since a sector-based agreement would actually be more complicated and less useful in the future. Ottawa’s suspicions that Ontario’s position was a delaying tactic may have been accurate. Manley reminded Lankin that “the PM and the Premiers...endorsed the June 30, 1994 deadline [at their FMM on 21 December]. I take this as a

⁴⁸³ PCO FOI request (A-2014-00381/JL): Doc. 3-0002-94RD(01)(C), 24 Jan 1994, “Record of Cabinet Decision,” p.3.

⁴⁸⁴ Archives of Ontario, Folder B501234 – CMIT January 19-29/94, “CMIT January 19-20: Meeting Scenario Note,” 18 January 1994, p.2. See also same folder, “Letter from Lankin to Manley,” 8 December 1993, p.2.

⁴⁸⁵ Ibid., p.5.

clear signal to us...to get on with it".⁴⁸⁶ Thus, HoG political impetus appears for a rare and brief moment. Klein in particular was "totally committed" to the objective of eliminating barriers.⁴⁸⁷

The January 1994 CMIT meeting succeeded in reaching a decision to conclude a rules-based agreement with caveats: it would be limited to only eleven sectors. Interestingly, the communiqué's wording was almost verbatim that of Lankin's pre-meeting note. The communiqué states "[Ministers] agreed that an internal trade agreement should be simple to understand, useful to business and labour and easy to administer...[whilst] ensur[ing] all governments can continue to set and maintain high standards in such areas as labour, the environment and the protection of consumers".⁴⁸⁸ The agreement to be drafted by chief negotiators should develop key rules, such as reciprocal non-discrimination, right of entry and exit, and reconciliation of standards – rules the sector chapters will then apply – as well as contain a dispute settlement system that does not involve the courts.⁴⁸⁹ The most contentious issue at this point was "around implementing the principle of reciprocity".⁴⁹⁰

After the meeting, Manley and Lankin were both satisfied with the direction of negotiations (McCarthy, 1994d). Yet Ontario and BC wanted as limited a scope as possible in order to forestall removing protective measures in sensitive sectors and to avoid constraints on their economic management abilities. Despite a strong public commitment to reducing barriers

⁴⁸⁶ Archives of Ontario, Folder B501234 – CMIT January 19-29/94, "Letter from Manley to Lankin," 12 Jan 1994, p.1.

⁴⁸⁷ Archives of Ontario, Folder B705175 – Communications: Other Provinces, "Letter from AB Deputy Premier Kowalski to Toronto Board of Trade," 4 January 1994, p.1.

⁴⁸⁸ Archives of Ontario, Folder B501234 – CMIT-January 19-20/94, "Press Release: Progress on Internal Trade Negotiations," 20 January 1994, p.11.

⁴⁸⁹ Archives of Ontario, Folder B501234 – CMIT-January 19-20/94, "CMIT Direction to Chief Negotiators," 25 January 1994, p.13.

⁴⁹⁰ Archives of Ontario, Folder B501234 – CMIT-January 19-20/94, "House Note: Comprehensive Internal Trade Negotiations," 4 March 1994, p.4.

to internal trade, the PM's brief stated that "these expectations [are] harder to realize. It will therefore be important for the federal government to maintain its low profile on this issue".⁴⁹¹

By February, negotiations were proceeding in the sector areas. Ontario was preparing a message plan containing two core issues: that the agreement be written "so it recognizes all these other tasks of govt [sic] first and then says we'll act on trade barriers to the extent that it doesn't take away from our primary obligations", i.e. economic development; and second, that "[Minister Lankin is] looking for new opportunities for jobs and markets. But she expects the benefits to be – of themselves – modest".⁴⁹²

The negotiations were proceeding but not without complaints.

It is hard to believe that the problems of interprovincial barriers are extensive and so serious that sensible people would adopt this draft agreement. I would predict that it could become a source of endless unnecessary [sic] conflict among jurisdictions rather than a means of dealing pragmatically with identifiable issues.

Ontario officials recognized the rules-based approach was an attempt to bind the bigger players:

some provinces may look at Ontario [just like Canada looks to the USA] and want to ensure that we are made subject to clear rules. Has this been a feature of the negotiations? If so, Ontario should not brush such concerns aside. Having said that,...a lack of precision in many of the 'rules' in this draft may provide plenty of opportunity for challenge and lengthy recourse to the dispute settlement procedures.

On that basis, "is it really too late to focus the exercise on what matters most?" As well, with regard to dispute settlement, it was felt that

the issues are political – leave the pressure on politicians to resolve problems rather than giving them the out of turning it over to panels etc etc.

⁴⁹¹ PCO FOI request (A-2014-00381/JL): Doc. 87619, "Memorandum to the PM: Barriers to Internal Trade, Outcome of CMIT Meeting," 24 January 1994, p.2.

⁴⁹² Archives of Ontario, Folder B705175 – Communications: Ontario, "Forwarded email from McGuire to Sadlier-Brown," 22 February 1994, p.10

Bearing in mind my earlier point about fears of the big guys (i.e. Ontario) it might be useful to have some sort of outside body that would consider a problem and recommend solutions to Ministers. But for heaven's sake not a panel that could 'make orders suspending a measure'...how does Knox think that a panel order will suspend a measure – i.e. alter a provincial law or regulation?

Ontario trade officials concluded "one could find an ample supply of potential landmines that have been spread around only because Knox and his fellow-conspirators want completeness rather than a more limited and pragmatic approach".⁴⁹³ Ontario believed "the General Rules of the draft Internal Trade Agreement limit provincial powers and could override the commitments made in the sector chapters".⁴⁹⁴ Indeed, its Ministry of Labour complained "the draft agreement in its present form does not seem to reflect the discussions at the sectoral table on labour mobility", particularly how to define 'no unnecessary obstacles' to freedom of movement. Ontario has high labour standards and the Ministry was concerned how those standards would fare under such a broad and subjective phrase.⁴⁹⁵

Québec's analysis of the agreement came to a similar conclusion: that the general provisions of the AIT were

susceptible de se révéler problématique...Cette complémentarité des articles 1, 2, et 3 de l'Accord paraît cependant moins évidente lorsque l'on s'attarde aux libellés mêmes de ces différents articles qui...sont susceptibles de se chevaucher l'un l'autre. La formulation de l'article 2, par exemple, est suffisamment large pour couvrir les mesures qui, directement ou indirectement par leurs effets, restreignent la libre circulation des personnes, des biens, des services et des capitaux".

⁴⁹³ Archives of Ontario, Folder B501234 – Text: Draft Secretariat Feb 14/94, "Email from Robert Johnstone to Sadlier-Brown and McGuire," 18 February 1994, p.1

⁴⁹⁴ Archives of Ontario, Folder B705175 – Communications: Ontario, "Communication Messages: Concerns with the Scope of the Internal Trade Negotiations," 25 March 1994, p.1.

⁴⁹⁵ Archives of Ontario, Folder B501234 – Text: Draft Secretariat Feb 14/94, "Memorandum from Labour Ministry, Employment Conditions and Labour Market Policy Branch to McGuire," 22 February 1994, p.1.

The report also noted “il faudra donc s'assurer que la notion ‘d'objectif légitime’ aménage pour les parties signataires à l'Accord suffisamment de latitude pour maintenir ou adopter des mesures qui sont, pour le Québec, jugées essentielles”.⁴⁹⁶

Both Ontario and Québec viewed the draft agreement as too broad, creating uncertainty for policy-makers. As their internal analyses indicated, they were unwilling to limit their ability to exercise policy-making powers on economic development in return for ‘endless conflict’. The principle of binding the ‘bigger’ players made sense to Ontario but only if enacted clearly and narrowly with as much control as possible retained by politicians. It was a position that flew in the face of the AIT’s goals of removing the arbitrariness of internal barriers, improving national economic decision-making, and avoiding inefficiencies.

To counteract provincial intransigence, Manley reiterated Ottawa’s arguments on the need for reform in a speech to the Toronto Board of Trade. His thesis was short and simple: “we agree that we must improve the competitiveness of our economy. To do that, we must work as partners...we must cooperate to compete”. As in Australia, the route to international competitiveness was seen to be a reformed economic union: “When our markets were sheltered from external competition by protection in the 10 to 20 per cent range, we could afford inefficiencies...Now, to compete in the world of NAFTA and GATT, Canada *must* have an efficient economy...When internal trade is inefficient, it imposes a terrible drag on international trade”. Manley thought the problem with internal trade had nothing to do with recognizing the problem’s existence. The problem was that “the politicians are ahead of the bureaucrats...It’s just

⁴⁹⁶ Québec Archives, Box 24 A 001 09-04-003B-01, File 2005-10-003\271, “Commentaire Généraux de la Direction Générale des Affaires Juridiques du Ministère de la Justice sur l’Accord Canadien sur le Commerce Intérieur,” 15 February 1994, p.5.

a fact that many civil servants, acting under previous political masters, created and nurture the very programs they are now being asked to modify or eliminate”. Manley ended his speech with some of the big questions that negotiators were about to answer:

Believe it or not, after nine months of negotiations there is still a question of whether we should have a set of hard-edged rules to govern future behaviour and to provide a meaningful basis for eliminating incompatible measures. Some governments are reluctant to commit themselves to the types of rules Canada has followed internationally for over 40 years – e.g. non-discrimination, no import or export controls, no disguised barriers. Second...there is a real reluctance on the part of some to give private parties...access to dispute resolution”.⁴⁹⁷

Manley may as well have pointed a finger directly at Ontario and its allies.

At the April 1994 CMIT meeting, the chasm between Ontario’s and Ottawa’s positions widened. Reconciling the general provisions with the sectoral negotiations was proving problematic: “There are subtle, but important differences in the world of the General Rules, that, in our view, make them difficult, if not impossible to apply [to the transportation sector]”. The proposed solution flipped the rules-based agreement on its head: negotiate each sector’s exemptions and then hope the general rules conform once finalized.⁴⁹⁸ Despite reports Ontario and the Atlantic Provinces had settled some of their disagreements at the meeting (McCarthy, 1994e), a mid-April editorial in the *Toronto Star* lamented the lack of progress, urging that “the Prime Minister should get involved” if the June deadline appeared to lapse. It supported Manley’s contention that “free trade at home is the only way to equip Canada for free trade abroad” and

⁴⁹⁷ Archives of Ontario, Folder B705174 – Communications: Canada, “Speaking Notes for the Honourable John Manley to the Board of Trade of Metropolitan Toronto,” 28 March 1994, p.5.

⁴⁹⁸ Québec Archives, Box 24 A 001 09-04-003B-01, File 2005-10-003\271, “Letter from Co-Chair Transportation Sectoral Negotiating Group to Mauro,” 16 March 1994, p.2.

excoriated the provinces for false economies of protectionism and granting Americans and Mexicans greater access to provincial markets than other provinces (Toronto Star, 1994a).

Seeing the potential for a less-than comprehensive agreement, Alberta shifted strategies and adopted Ontario's rhetoric of promoting the interests of the corporate sector. It then argued that limiting the agreement to eleven sectors was not the original intention of Ministers.⁴⁹⁹ Alberta wanted a rules-based approach covering all sectors whilst Ontario sought limitations. Saskatchewan shared Ontario's skepticism regarding a rules-based approach because of the impact on its Crown corporations but was moving towards accepting an agreement with certain exemptions. BC strongly supported Ontario's sector-based approach, although "BC is more interested in attacking Alberta than in resisting the federal government".⁵⁰⁰

The result of these shifts was a confirmation of the "federal view that it has succeeded in isolating Ontario". The Ontario government was especially concerned that "the federal government is not doing a good job in managing public expectations of this process. The agreement which will be signed does not so much remove a list of specific barriers as it sets in place a series of structures and work plans for future activities." Ontario believed "the agreement suggests the creation of on-going fora of ministers – both sectoral and trade ministers...In this way, the agreement will continue to be improved".⁵⁰¹

Thus, even the most skeptical party acknowledged that the economic reform programme was also aimed at institutional change. The changes were directed at reforming the CMIT, much

⁴⁹⁹ Archives of Ontario, Folder B501234 – CMIT-April 5-6/94, "CMIT Halifax: Meeting Scenario Note," 31 March 1994, p.10.

⁵⁰⁰ Ibid., p.4.

⁵⁰¹ Ibid., p.10.

like an agreement on the environment institutionalized the Canadian Council of Ministers for the Environment. With all these ministerial councils experiencing institutionalization, FMCs may have been next on the reform agenda.

Even after the AIT was signed, Ottawa and its allies continued to push for institutionalization. Ontario noted that Alberta and Ottawa were

“trying to regain lost ground in the main negotiations by: pushing for a large, activist ITS that will play a strong policy and advocacy role which goes beyond that mandated by the Agreement; seeking an overly formalized and legalistic dispute settlement process; and,...enhanced status for private parties in dispute settlement proceedings”.⁵⁰²

Ottawa’s proposal called for creating a non-profit corporation – similar to the Council of Ministers for the Environment – that would conduct all CMIT affairs and supervise the ITS, thereby “merging political and administrative decision making”, which would be based on majority voting by a “small executive committee, rather than by all directors”.⁵⁰³ This would raise the level of routinization to a medium level, with strong density of contacts, regular meetings, and an autonomous supporting organization.

Yet Ottawa’s proposal did not conform to the other provinces’ premise for institutionalization: “a structure for the institutional and dispute settlement mechanisms of an [AIT] based on the criteria of ‘cheap, quick and effective’”.⁵⁰⁴ Specifically, Ontario wanted a “clearinghouse for information, with a small staff supporting the [CMIT]...to avoid the creation of

⁵⁰² Archives of Ontario, Folder B705175 – CMIT Meeting April 11-12/95, “CMIT Calgary: Meeting Scenario Note,” 7 April 1995, p.2.

⁵⁰³ Archives of Ontario, Folder B705175 – CMIT Meeting April 11-12/95, “Minister’s Background Note: Framework for the CMIT and the Secretariat,” 7 April 1995, p.1.

⁵⁰⁴ Alberta FOI request (2015-G-0007): Applicant Package Part 1, “Institutional Arrangements and Dispute Settlement Procedures,” 12 November 1993, p.310.

an independent voice over which Ministers have no effective control”.⁵⁰⁵ Saskatchewan believed the ITS “should have its primary focus in supporting internal trade representatives and not in replacing [their] individual and joint responsibilities to federal and provincial Ministers”,⁵⁰⁶ whilst Québec wanted a “mécanisme de prise de décision semble préférable et conforme à l’esprit de recherche de compromis qui a guidé nos gouvernements tout au long du processus de négociation de l’[AIT]”.⁵⁰⁷ Without an autonomous supporting organization, provinces were backing a weak level of routinization. The debate was criticized by the The Canadian Chamber of Commerce (1996, p. 20) for slowing the pace of progress.

Even by 1998, the provinces and Ottawa were still debating the regularity of CMIT meetings. Ontario wrote to Manley requesting a CMIT meeting for November 1998: “[the meeting] could be a positive way to bring Ministers together in cooperative ventures. We have spent a long time negotiating various issues...and there remain several issues for negotiation. However, at this time I sense a general negotiating fatigue among our [CMIT] colleagues”.⁵⁰⁸

Ontario’s request here for political impetus is a pattern that played out many times during the course of the AIT negotiations. HoG announce their goals and issue a mandate to Ministers. The mandate is found to be inadequate to deal with politically sensitive issues like Crown corporations, regional development, energy policy, and government procurement. Rather than escalate the issue to HoG, who could negotiate across all these issues, the chief and sectoral

⁵⁰⁵ Archives of Ontario, Folder B705175 – CMIT Meeting April 11-12/95, “Memorandum from McGuire to Lankin,” 21 February 1995, p.1.

⁵⁰⁶ Archives of Ontario, Folder B705175 – CMIT Meeting April 11-12/95, “Letter from SK Economic Development to Knox,” 3 March 1995, p.1.

⁵⁰⁷ Archives of Ontario, Folder B705175 – CMIT Meeting April 11-12/95, “Letter from Line Gagné, Coordonnatrice interministérielle Groupe sur le commerce intérieur, to Chief Negotiators,” 10 March 1995, p.1.

⁵⁰⁸ Industry Canada FOI request (A-2014-00440_0001), “Letter from Palladini to Manley,” 14 Sept 1998, p.49.

negotiators are left to battle it out amongst themselves until either Ministers intervene and reach a narrow compromise or the issue is dropped and left for another day.

From Ontario's perspective, institutionalization was unrelated to the practicalities of the AIT, including its implementation, expansion, and deepening:

Focusing on practical initiatives offers the opportunity to develop Parties' common interest in economic development...We have also been developing new tools for businesses to use to improve their competitiveness and to increase their markets. I think it would be good to share these ideas...Important concepts for us to focus on when we consider new approaches for practical initiatives are voluntary participation and flexibility.⁵⁰⁹

Manley responded to Ontario's request for a meeting.

I must confess to some disappointment at your sense that [CMIT] colleagues are experiencing negotiating fatigue. There is much that we have not done that we have said we would do...At our last meeting, we agreed that jurisdiction be asked to identify ways of improving the Agreement in advance of the last Annual Premiers' Conference. Unfortunately, I understand that only the federal government and more recently Ontario have advanced proposals in this regard...Ontario's proposal that we concentrate on practical initiatives could be further defined and advanced within this context...It is not clear to me, however, how some of these [practical initiatives] relate to the AIT and what advantages there may be from bringing them under this umbrella. I would hope that any emphasis we might wish to place on such initiatives would not detract from the need to address as well some of the more structural issues under the Agreement.⁵¹⁰

Ontario's response came at the end of November, at which point the next CMIT had been pushed back to either February or March 1999: "I think that establishing a regular annual [CMIT] meeting early in the year would help to focus our activities and contribute to greater progress on internal trade issues". Thus, the institutionalization of the CMIT ministerial council – supported by the ITS, an independent secretariat – was thwarted by provincial desires to retain complete authority and

⁵⁰⁹ Industry Canada FOI request (A-2014-00440_0001), "Letter from Palladini to Manley," 9 October 1998, p.51.

⁵¹⁰ Industry Canada FOI request (A-2014-00440_0001), "Letter from Manley to Palladini," 29 October 1998, p.46.

exclusive control over policy-making. With little value infusion and routinization, IGR on internal trade remained weakly institutionalized.

The AIT's agenda for microeconomic reform engaged the mechanism of continuous negotiation, which eventually managed to move negotiations towards improving policy-making structures and rules. Ministers sought to formalize the regularity of their ministerial council, perhaps the most basic form of routinization.

Yet provincial reluctance to negotiate a comprehensive deal would thwart the mechanism's ability to expand negotiations beyond microeconomic reform: "In terms of issues dividing the camps, we have seen significant backtracking from the positions supposedly settled by ministers in January", including whether the agreement is rules-based or sector-based and whether dispute settlement is via negotiations between governments or an elaborate process involving private parties. Ontario's proposed solution was working: "our problems are being addressed by modifying the rules in the sector chapters",⁵¹¹ within which Ontario felt it could achieve "a careful examination of what special problems may arise out of the application of general rules".⁵¹² Those special problems, i.e., anything that could limit its policy-making abilities, prevented the mechanism from fulfilling its potential, which the next section examines in greater detail in order to specify the linkage between the archive files and the political economy data.

⁵¹¹ Archives of Ontario, Folder B501234 – CMIT-April 5-6/94, "CMIT Halifax: Meeting Scenario Note," 31 March 1994, p.3.

⁵¹² Ibid., p.9.

Regional Development

Regional development was one of the major reasons that provinces cited in their opposition to the AIT; it surfaced again and again in provincial and federal documentation. The issue first emerged when provinces and Ottawa were negotiating the AIT's mandate. Eventually, parties reached a compromise to include regional development in the negotiations. Ontario wanted

to have 'economic development' removed from the list of sectors arguing that provincial governments wanted to retain the ability to provide incentives for regional development...and suggested incentives for regional development purposes should [sic] be outside any review of internal barriers. Bob [Knox] insisted that economic development incentives needed to be left on the table but was willing to consider removing them as a sector but having it understood that they could be part of the discussions in each group. This was the compromise.⁵¹³

The issue was also present as parties discussed the AIT's basic framework. In Wilson's memorandum to Cabinet, the AIT would secure freer internal trade via certain rules, the first being that all parties commit to ensuring equal competitive opportunities. This was followed by a ban on measures that decrease access to provincial markets, then transparency regarding measures that may impact internal trade, and finally harmonization or, failing that, mutual recognition. As is now known from the Australian case, mutual recognition is a workable compromise in federal systems owing to its preservation of provincial autonomy whilst unencumbering trade and market access. However, mutual recognition was not successfully implemented in Canada.

⁵¹³ Archives of Ontario, Folder B501234 – Meeting: Chief Negotiators-Task Force of Officials on Internal Trade, "Email from Wright to McGuire: The comprehensive process begins," 18 December 1992, p.3.

One problem with mutual recognition – or reciprocal non-discrimination in the language employed by negotiators – was that it would reduce provincial control over access to their market. One of the purposes of regional development incentives is to support local firms directly, which requires limiting outside firms' access. The federal government noted at the March 1994 CMIT meeting that regional development is

a constitutional responsibility. Quebec wants an economic development exception and will not accept any limitations on its ability to attract or develop firms. Ontario feels any exceptions should be contained within the sectoral agreements [because it] allows all Parties to expand or contract their market access in response to changing conditions and ensures the continuation of a mutually acceptable and balanced agreement.⁵¹⁴

Ontario sought sector exemptions rather than a blanket regional development exemption: “[we] will reject any agreement that cracks open [Ontario’s] market while other provinces can continue to erect trade barriers...Right now...there’s a big line-up for exceptions put on the table by other provinces. [Lankin] would like to see them limited” (J. Ferguson & McCarthy, 1994). At the March 1994 CMIT meeting, Ontario conceded that it “has received no support for our principle of reciprocal non-discrimination. We need to shift our ground and appear to give on this issue”.⁵¹⁵ The federal language on the issue sought to treat all Canadians the same, which Ontario believed also meant “greater access for foreign firms”,⁵¹⁶ whereas Ontario’s language sought to “extend favourable treatment only to Parties who reciprocate”.⁵¹⁷

To prevent foreign firms from using the AIT to enter the Canadian market, provinces sought a blanket exemption for foreign firms seeking rights under the AIT. Otherwise, the AIT

⁵¹⁴ Archives of Ontario, Folder B501234 – CMIT-April 5-6/94, “CMIT Halifax: Meeting Scenario Note,” 31 March 1994, p.13.

⁵¹⁵ Ibid., p.2.

⁵¹⁶ Ibid., p.8.

⁵¹⁷ Ibid., p.7.

“may cause us to ‘back into’ new international obligations we had not intended”.⁵¹⁸ Opening access to provincial markets was already proving difficult and provinces did not want to extend preferential treatment to non-Canadians, especially where regional development was concerned. International access to the Canadian market was best dealt with via international agreements, negotiations on which provinces had a consultative role that they expected would continue.⁵¹⁹ A report to Industry Canada from the office of Goodman & Goodman stated emphatically that the AIT “does not grant new rights to any of Canada’s international trading partners or impose new obligations on either Canada or any province respecting such trading partners”.⁵²⁰ The Europeans thought otherwise. During a meeting of Canadian and EU officials held under the auspices of the 1976 Framework Agreement for Commercial and Economic Cooperation, EU officials noted that they “expected ‘good news’ from the [internal trade] negotiations; the implication being that EU producers would benefit from any offer made to other provinces because of the international obligation to provide best in-province treatment...The EU representative restated his opinion that the internal trade negotiations might be a useful vehicle for change”.⁵²¹

Ontario’s response to the reciprocal non-discrimination situation was two-fold. On the one hand, it agreed with the other provinces that it was not about to constrain its policy-making powers to a large degree, a position that targeted Ottawa and the NDP’s constituency. At one point, officials were briefed that “labour and social policy groups have entered the public debate,

⁵¹⁸ Ibid., p.8.

⁵¹⁹ AIT Article 1809 (4), Internal Trade Secretariat (2015).

⁵²⁰ Alberta FOI request (2015-G-0007): Applicant Package Part 2, “Re: Agreement on Internal Trade, Goodman & Goodman to Asst Deputy Minister of Industry von Kinckenstein,” [no date], p.389.

⁵²¹ Archives of Ontario, Folder B705175 – CMIT Meeting-June 27-28/94, “Background Note: Meeting of Canada-EU Joint Cooperating Committee,” 10 May 1994, p.1.

questioning the need for an internal trade agreement and focusing on their concern that such an agreement will weaken the role of provincial governments in protecting workers, communities, and the environment”.⁵²² Ontario’s response was that lowering standards and full-scale national harmonization were not in its interest and were not up for negotiation. It went further in addressing labour’s concerns, describing the AIT as “simply mak[ing] trade one consideration to be taken into account in maintaining standards, extending environmental protection, and assisting in economic development”.⁵²³

The second response was directed at the other provinces. Premier Rae stated that “[Ontario] is willing to make equalization payments, but not to have every national policy and program tilt against [it]” (McCarthy, 1994c). It must be noted that the provinces do not ‘make’ equalization payments; they come from federally-collected taxes. It is likely that Rae’s comment is shorthand for the fact Ontario taxpayers contribute more to the federal tax pool than they receive from it, which was the reason behind his government’s review of fiscal federalism. The Ontario government calculated in 1991 that Ontarians contributed 43% of total federal taxes and received only 28% of all subsidies to industry and only 27% of federal spending on industrial assistance. The remainder of the money is spent “to attract the production facilities and employment out of Ontario...Ontario residents are paying a large portion of the federal taxes that are being used against them” (quoted in Hall, 1998, p. 69). Naturally, the other provinces

⁵²² Archives of Ontario, Folder B501234 – CMIT-June 6-7/94, “House Note: Comprehensive Internal Trade Negotiations,” 8 June 1994, p.1. See Canadian Centre for Policy Alternatives report entitled “Shifting Power, Depressing Standards.”

⁵²³ Archives of Ontario, Folder B705175 – Consultations with Private Sector, “Response to ‘Shifting Power, Depressing Standards’: Prepared by Ministry of Economic Development and Trade,” 24 June 1994, p.1.

countered with the 120 years of benefit that Ontario received from the National Policy at their expense.

On that note, BC requested at the May 1994 CMIT that

natural resources should be excluded from the agreement to ensure the effective management of the provinces non-renewable natural resources....The support for the exclusion of natural resources has been growing within the Natural Resources Processing sector table. BC is the strongest proponent for excluding natural resources from the agreement. The Ontario Ministry of Natural Resources is also strongly in favour of excluding natural resources from the agreement.⁵²⁴

Provincial control of natural resources is another major component of regional development since every province's major export industries are tied to natural resources, with the exception of Ontario and Québec. Exempting natural resources supported a regional/provincial policy orientation, which seeks to maintain provincial competitiveness by limiting market access. These internal barriers would be maintained via exemptions to the AIT's general rules. BC was already competing with the USA and Asia, why would it add Ontario to the mix? It is worth quoting again BC Minister Zirnhelt: "We want to...expand trade with Canada. But if the trade is so free that it means raw materials will flow to the industrial heartland, we would have to be cautious about the effects it would have on this region".⁵²⁵ From BC's point of view, reciprocal non-discrimination could interfere with its ability to manage its resources, control its own market, and engage in economic development. Its overwhelming reliance on international trade created

⁵²⁴ Archives of Ontario, Folder B501234 – CMIT-May 9-10/94, "CMIT Winnipeg: Meeting Scenario Note", 6 May 1994, p.6.

⁵²⁵ Archives of Ontario, Folder B501234 – Meeting: Chief Negotiators-Task Force of Officials on Internal Trade, "Media Analysis March 18 CMIT Meeting for Internal Trade," 2 April 1993, p.2.

an incentive for BC to retain economic policy independence. Mutual recognition requires a pooling of sovereignty that was politically unacceptable at the time.

Even though BC and Ontario were both governed by the NDP at the time, it is unsurprising that on the regional development issue they held opposite positions: “Premiers from slow-growth provinces consistently argue for greater regional development efforts, while premiers from the more developed provinces consistently argue for less federal-government intervention in the name of regional equity” (Savoie, 1992, p. 4). Rather than partisan conflict, regional development fosters federal-provincial tensions: “regional development has often been a pawn in the continuing struggle between ‘nation-building’ and ‘province-building’” (ibid., p. 15). During the negotiations, Manley heavily criticized the scope given to protecting regional development policies and tried to acquire the intervention of HoG (D. Brown, 2002, p. 157).

Adding to the problem was the issue of government procurement, which Ottawa uses “for industrial and regional development purposes” and which is exempt from non-discrimination rules. The provinces themselves disagreed on whether the exemption should continue, with Ontario wanting it to end and the Atlantic Provinces concerned about “the federal government [using] the agreement to cut off federal economic support to their region”. The May 1994 CMIT meeting instructed negotiators “to determine the extent to which regional and economic development exceptions are required in the eleven sector...chapters”.⁵²⁶ According to Ontario’s negotiators, “the debate rages over 2 days...[T]he point is to get the Atl[antic Provinces] off the idea that reg dev [sic] will be torn asunder unless the feds [sic] are given an unqualified carve-

⁵²⁶ Archives of Ontario, Folder B501234 – CMIT-May 9-10/94, “CMIT: Summary of Decisions,” 10 May 1994, p.2.

out”.⁵²⁷ The issue was one “which the federal government will have to resolve with the Atlantic provinces directly. [Ontario] share[s] the same position taken by BC and Quebec that the provinces and the federal government have the same ability to undertake activities for regional and economic development”.⁵²⁸ Ontario was unconcerned because its “industrial policy does not rely on preferential procurement because it is often an ineffective policy lever and inefficient for economic development. When we need to use procurement policy, we will be able to do so”.⁵²⁹

Ironically, Ontario was simultaneously receiving complaints about the local procurement policies of Québec. The Director of the Ontario Pollution Control Equipment Association (representing sales of \$2.5 billion at the time) “asserted that the purchasing policies and procedures of the Government of Quebec promote unfair trade practices”.⁵³⁰ If Québec can use local procurement as an economic development tool, than so should Ontario. This is despite a report to Manley that noted

while most delegations recognized, during the negotiations last year, that procurement was an inefficient regional or economic development tool it was not possible to achieve any consensus on not including it as a justification for departing from the procurement procedures”.⁵³¹

The *Toronto Star* reported that BC, Québec, and Saskatchewan wanted their own Crown corporations excluded from the general principle, thereby allowing them to favour local

⁵²⁷ Archives of Ontario, Folder B501234 – CMIT-May 9-10/94, “Email from McGuire to Ontario Sector Negotiators,” 11 May 1994, p.2.

⁵²⁸ Archives of Ontario, Folder B501234 – CMIT-May 9-10/94, “CMIT Winnipeg: Meeting Scenario Note”, 6 May 1994, p.4.

⁵²⁹ Archives of Ontario, Folder B705175 – Consultations with Private Sector, “Response to ‘Shifting Power, Depressing Standards’: Prepared by Ministry of Economic Development and Trade,” 24 June 1994, p.3.

⁵³⁰ Archives of Ontario, Folder B705175 – Consultations with Private Sector, “Background note: Meeting with Ontario Pollution Control Equipment Association,” 11 August 1993, p.1.

⁵³¹ Industry Canada FOI request (A-2014-00391_0001), “Procurement – MASH Provisions: Rules-Based Text-Substantive Issues,” 24 November 1995, p.86.

suppliers: “Sources close to the talks say [that]...‘Ontario is a born-again free trader in this case...Ontario has the largest manufacturing capacity so it would benefit the most’” from dismantling regional development (McCarthy, 1994a).

The preceding review demonstrates that the political economy of regional development in Canada proved to be a major factor influencing the AIT negotiations. Atlantic Provinces desperately sought regional development exemptions whilst BC, Ontario, and Québec “will not accept an agreement which does not provide both orders of government with the same ability to use non-conforming measures for regional and economic development”.⁵³² Ontario was forced into this position by provinces that refused to accept reciprocal non-discrimination. Ottawa was caught in the middle, with Manley wanting an end to all exemptions but having to recognize Ottawa’s constitutional (and political) responsibility for regional development. As such, it was forced away from its position as equal partner during the negotiations despite the presence of the neutral chair. It had different relationships with different provinces both historically and politically. The more the provinces disagreed with each other, the more Ottawa was forced to intervene to reach an agreement. Just as Keating’s heavy-handed intervention in the SPCs almost scuttled the entire process, so too Ottawa’s intervention increased the possibility of failure. Canada’s economic and political complexity demanded central intervention in order to bring the negotiations to some sort of conclusion.

The key to understanding the disagreement on these issues is that province-building, i.e. a regional/provincial policy orientation, is a key role of practically every province. In addition, the

⁵³² Archives of Ontario, Folder B501234 – CMIT-May 9-10/94, “CMIT Winnipeg: Meeting Scenario Note”, 6 May 1994, p.2.

goal of the peripheral provinces and even Québec is to close their gaps with Ontario. Whether it be to diversify economies or promote growth in existing sectors, regional development sees governments take an “activist approach [that] makes intergovernmental cooperation considerably more difficult, and it also increases the likelihood of conflict” (Savoie, 1992, p. 17). Since provinces do not control important macro-economic policy levers (such as monetary policy), they “have to be very focused on what they can do. We can promote a climate for investment, we can promote good education, we can promote good infrastructure...But beyond that [there is] an exaggerated sense of what [provinces] can achieve” (Bob Rae quoted in Hall, 1998, p. 257). The effect is that provinces, and even federal ministers from specific regions, no longer accept a ‘national’ policy orientation as the main priority of economic policy despite the failure of decades of effort and billions of dollars to eliminate regional disparities. The overall result is that regional development

has been a roller-coaster ride of experimentation infused with the vicissitudes of political theatrics, theoretical fads, and ideological pendulum swings. It is the quintessential manifestation of regional and federal politics in a highly fragmented and controversial institutional system such as Canada (Conteh, 2013, p. 67).

For Ottawa then, regional development is a Gordian knot. Different provinces want it to be fully involved or to withdraw. Ottawa’s constitutional responsibility for regional development must be balanced with its responsibility to sustain the economic union. When regional development policies conflict, Ottawa must intervene for the sake of the national economy – a task specifically noted by the Macdonald Commission – yet doing so exacerbates regional tensions and curtails national policies, just as it curtailed Ottawa’s effort to secure the AIT.

Ottawa's problem has three elements. First, there is a realization that macro-economic policies are not sufficient to promote growth in all regions (McMillan, 1989). This leads to the second element whereby resource-rich provinces spend on projects that make little sense from the point of view of national strategic economic development (Boadway, 2007; Leslie, 1987). National economic policy-making is thus doubly constrained. Indeed, the Mulroney government decentralized regional development institutions – locating them outside Ottawa and granting them policy autonomy – in order “to accommodate the emergence of a new wave of assertive provincialism marked by increasingly strong, willful provincial governments and local interests bent on pursuing locally defined economic strategies” (Conteh, 2013, p. 68). The third aspect of the problem is that “Canadians have made it clear that they expect their federal government to take responsibility for improving regional economies and they are not deterred by arguments of constitutional jurisdiction” (McGee, 1992, p. 25).

Savoie (1992), Courchene and Melvin (1986), and the Macdonald Commission all suggest that federal regional development policy should seek to integrate provincial economies into at least the regional economy, and the national economy when possible. But provinces “tend to view economic development as a ‘zero-sum game’ in which the winners are identified on a case-by-case basis and in highly regional terms” and want Ottawa to fairly distribute economic activity throughout the country (Savoie, 1992, p.232). Doing so requires clear goals and objectives, and difficult policy decisions, which invariably leads to conflict.

Further eroding Ottawa's influence were the very free trade agreements it was negotiating as it switched from a national policy orientation to a liberal-continentalist one. According to Watts (1990, p. 162), free trade imposes limitations on policies within federal

jurisdiction “leaving important areas of provincial jurisdiction including education, training and industrial relations and social services undiminished”. Yet “for Ottawa to vacate the field completely would provoke bitter regional tensions and probably give rise to all kinds of ‘me first’ provincial economic initiatives” (Savoie, 1992, p. 232). For Savoie (*ibid.*, p. 242), it is no surprise that regional development policy is highly political and therefore subject to sudden changes of direction. The tension is exacerbated as provinces further integrate into their regional American markets. Secured to their most important market to the south, provinces are at liberty to protect their markets from out-of-province competition and see no urgency in taking the risk of cooperating to reform their economies and open them to further competition. However, such a position favours short term gains – which Mandel-Campbell (2007) described as the ‘low-hanging fruit’ of profiting from regional American markets – rather than long term economic adjustment. Most practitioners conclude that regional development policies at least prevented regions from falling further behind but that the policies themselves did little to actually reduce disparities in growth or unemployment (McGee, 1992; Savoie, 1992).

It is clear that regional development interfered with the completion of a rules-based, comprehensive AIT. The desire for policy manoeuvrability – and the exemptions to the general rules that facilitated it – could not be reconciled with the general principles governing internal trade and market access. Provincial political economies incentivized less generality in rules and less domestic market openness – i.e., the imposition of sectoral exemptions – in order to protect their economic policy capabilities in the context of a liberal/continentalist policy orientation. The result is an incentive to compete that overwhelmed the attempt to cooperatively govern the economic union.

A compromise on regional development was eventually reached that secured the AIT in time for the June 1994 deadline. Despite Manley's own criticism of the scope of the exemptions to the AIT's general rules, Chrétien was informed after the May CMIT meeting that Manley was "ready to accept an agreement covering less than eleven sectors, as long as the framework for the agreement (i.e. rules, operating principles, institutional provisions and dispute settlement procedures) represents significant progress towards the elimination of trade barriers. CMIT could then establish a new process to negotiate individual sectoral chapters".⁵³³ In other words, Manley was ready to perpetuate the mechanism of continuous negotiation past the negotiations' deadline in the hopes that eventually the provinces would agree on further reforms. Having failed to either reach a comprehensive deal or expand the reform process, it was hoped time would finally allow the mechanism to function.

The 6 June CMIT meeting was in "large part...taken up with the discussion of a regional/economic development exception" as well as on specific exemptions. Québec noted that the Atlantic Provinces especially wanted to maintain certain specific exemptions on alcohol, which it noted "ne soient pas traités comme des exceptions permanentes mais comme des mesures non conformes assujetties à un processus de révision et à une date d'extinction".⁵³⁴

Eventually, a compromise was reached on regional policy exemptions, which centred on how to define regional development: "a government cannot simply call a local preference a 'regional development measure' – there has to be an actual program, framework criteria".⁵³⁵ The

⁵³³ PCO FOI request (A-2014-00381/JL): Doc. 94036, "Memorandum to the PM: Status of the Internal Trade Negotiations, 31 May 1994, p.3.

⁵³⁴ Québec Archives, Box 24 A 001 09-04-003B-01, File 2005-10-003\271, "CMIT 6-7 June 1994: compte rendu et suivi à donner," 10 June 1994, p.2.

⁵³⁵ Archives of Ontario, Folder B501234 – CMIT-June 6-7/94, "Memorandum to Internal Trade Sectoral Negotiators from McGuire re: June 6-7 CMIT," 8 June 1994, p.1.

provinces would then be required to report annually on such programs. They also agreed that the privatization and sale of Crown assets would not be covered by non-discrimination provisions.⁵³⁶ Québec noted it was able to “obtenir des exceptions relativement larges au niveau du développement économique, du développement économique régional, de la culture et par l’exclusion des sociétés d’État de la partie de ce chapitre [d’investissement]”.⁵³⁷ However, regarding the general exemption for regional development, Québec was largely unhappy that discussions were incomplete:

Monsieur [Gérald] Tremblay a fait ressortir à plusieurs reprises lors de la discussion portant sur cette questions les particularités de la politique québécoise en matière de développement économique régional. Il a posé à M. Manley la question de savoir dans quelle mesure l’approche du Québec était compatible avec les propositions émises. Ce dernier a alors affirmé qu’il ne voyait pas d’incompatibilité dans l’approche québécoise avec la définition de la clause d’exception.⁵³⁸

Eventually Québec accepted the compromise.

As compensation for the regional development carve out, which went against its reciprocal non-discrimination premise that it would open its market to the other provinces if they opened their markets, “Ontario wants more access in procurement” in order to agree to a final deal. Otherwise, “an open-ended exclusion for regional and economic development programs could compromise Ontario’s ability to portray the agreement as achieving significant market access gains for Ontario firms and workers”.⁵³⁹ By the end of the meeting, “most seem content

⁵³⁶ Québec Archives, Box 24 A 001 09-04-003B-01, File 2005-10-003\271, “CMIT Fredericton: Summary of Decisions,” 7 June 1994, p.2.

⁵³⁷ Québec Archives, Box 24 A 001 09-04-003B-01, File 2005-10-003\271, “CMIT 6-7 June 1994: compte rendu et suivi à donner,” 10 June 1994, p.2.

⁵³⁸ Ibid., p.5.

⁵³⁹ Archives of Ontario, Folder B501234 – CMIT-June 6-7/94, “CMIT Fredericton: Meeting Scenario Note,” 5 June 1994, p.4.

to describe the deal as a 'modest and useful first step', placing emphasis on the continuing discussion mandated within the sectoral chapters and through CMIT. Only Alberta continues to express dissatisfaction with the package as a whole".⁵⁴⁰

By 24 June, all was falling apart: "We understand that negotiations on internal trade barriers are regressing, and that several provinces are backsliding on issues which were previously agreed to".⁵⁴¹ Ontario confirmed that Ottawa was "highly critical of the sectoral negotiations...In the federal view, the sectoral agreements...are 'weak' and will compromise the comprehensiveness and marketability of the agreement". Ontario was prepared to "derogate from the obligation...to extend the best treatment to all Parties if the Agreement does not result in reciprocal benefits for Ontario".⁵⁴² Ontario also stated that Québec was beginning to have reservations, particularly with national standards and economic development. Manley described the current state of negotiations as "below a credible deal" with Québec having "shifted from that of being supportive of a comprehensive agreement, to being totally inflexible and demanding".⁵⁴³ Québec's own report on the negotiations, dated 1 June, indicated its reservations regarding regional development and its ability to intervene:

De fait, hormis la proposition visant à limiter les aides qui pourraient avoir pour effet de délocaliser une entreprise d'une autre province, les propositions...conduiraient à une limitation importante de la marge de manoeuvre du gouvernement québécois dans ses politiques de développement

⁵⁴⁰ Archives of Ontario, Folder B501234 – CMIT-June 6-7/94, "Memorandum to Internal Trade Sectoral Negotiators from McGuire re: June 6-7 CMIT," 8 June 1994, p.4.

⁵⁴¹ PCO FOI request (A-2014-00381/JL): Doc. 94668, "Memorandum to the PM: Internal Trade Barriers – Federal Options, 24 June 1994, p.1

⁵⁴² Archives of Ontario, Folder B501234 – CMIT-June 22/94, "CMIT Toronto: Meeting Scenario Note," 21 June 1994, p.3.

⁵⁴³ PCO FOI request (A-2014-00381/JL): Doc. 94668, "Memorandum to the PM: Internal Trade Barriers – Federal Options, 24 June 1994, p.1.

industriel. Au chapitre de l'aide au développement régional, une exception est prévue.⁵⁴⁴

At this point, Ontario was forced to resume its traditional role as peacemaker in the federation; it was “putting forth some sound compromise wording..., but Quebec consistently rejected suggestions...Mr. Manley is concerned that the negotiations are leading to a trade war between the two provinces”. Manley then enlisted the assistance of Marcel Massé – then Minister of Intergovernmental Affairs and PM Chrétien’s Québec lieutenant – who intervened with Premier Daniel Johnson to secure an agreement. It seemed the Premier’s Office was not being kept informed of CMIT discussions and that Québec’s intransigence would have to be removed directly from the top.⁵⁴⁵ Further complicating matters was Alberta’s threat to walk away from the whole process because BC and Saskatchewan were demanding more exemptions for Crown corporations.

The desire to reach an agreement became even more urgent because the window of opportunity to reach a deal could close “once Mr Axworthy’s social reform paper is made public”.⁵⁴⁶ Then Minister for Human Resources Development, Lloyd Axworthy’s 18-month review “was a mammoth project aimed at reconstituting the unemployment insurance system, post-secondary education funding, and social assistance, with special focus on child poverty” (L. Martin, 2003, p. 105).⁵⁴⁷ Clearly at this point, a whole of government approach was not operating at either the provincial or federal levels. Ottawa’s perception that the window of opportunity

⁵⁴⁴ Québec Archives, Box 24 A 001 08-05-005B-01, File 2005-10-003\273, “Memorandum: Le chapitre de l’investissement dans l’Accord pan canadien, 1 June 1994, p.2.

⁵⁴⁵ PCO FOI request (A-2014-00381/JL): Doc. 94668, “Memorandum to the PM: Internal Trade Barriers – Federal Options,” 24 June 1994, p.2.

⁵⁴⁶ Ibid., p.4.

⁵⁴⁷ See also Greenspon and Wilson-Smith (1996).

was closing proved accurate. Draft comments for a press conference with Bob Rae were skeptical of Axworthy's paper and doubted Ottawa would follow through on its commitments.⁵⁴⁸

The AIT was supposed to be about creating jobs, reducing deficits, and increasing competitiveness, not protecting old policies that had not addressed Canada's long term economic problems. Rather than an agreement covering internal trade, the AIT should have been called the 'Agreement on the Legitimate Exercise of Provincial Sovereignty'. On the eve of the negotiating deadline, Manley stated that even though the agreement was partial – i.e. watered down – all parties would agree to it. Indeed, "this is the first step in negotiations that will continue," [Manley] said. 'I think the key is going to be whether we create a framework which will be a good base for future negotiations'" (A. Thompson, 1994). Continuous negotiations were certainly needed. In order to reach a deal before 30 June 1994, the deadline for agreement in certain sectors – agriculture, energy, and alcohol – was postponed by one year (D. Ferguson, 1994).

At the CMIT meeting on 28 June, Ministers announced they

have reached agreement-in-principle on the major policy issues required for a comprehensive agreement on internal trade...Canadians will have for the first time since Confederation: a rules-based system for trade within Canada; a dispute settlement mechanism...; a standstill on new barriers; commitments to future negotiations to broaden and deepen the Agreement; a code of conduct to prevent destructive competition for investment; more open government procurement; increased labour mobility; and a commitment to reconcile standards.⁵⁴⁹

Accompanying Ontario's workings on the final draft was a list of issues for future negotiations: extending the AIT to the municipal, academic, social services, and hospital (MASH) sectors,

⁵⁴⁸ Archives of Ontario, Folder B376382 – Intergovernmental Affairs (MIT) 1994, "Comments for press conference regarding the release of the Axworthy paper on social policy reform," 5 October 1994.

⁵⁴⁹ Archives of Ontario, Folder B501234 – CMIT-June 27-28/94, "Press Release: Internal Trade Negotiations: Agreement-in-Principle," 28 June 1994, p.1.

implementing labour mobility, concluding an energy chapter, and finalizing transportation standards.⁵⁵⁰ Even though the mechanism of continuous negotiation did not achieve significant reform to HoG decision-making, it would at least continue and operate much like the rest of Canadian IGR: ad hoc and irregularly.

According to the *Toronto Star*, even though citizens supported free trade in principle, they were unwilling “to see their governments yield the levers that could counterbalance the free market forces, which don’t always work to the benefit of local citizens”. In a period of economic distress, the medicine was too difficult to swallow. The result was “a pragmatic document that reflects the kind of compromises required to keep the unwieldy Canadian federation wheezing along”. According to media sources, Manley was the AIT’s chief architect and kept the provinces on track; “Manley was less interested in ideology than his Tory predecessor and more interested in practical results dealing with the worst of the barriers without insisting provinces give up all their economic powers” (McCarthy, 1994b).

The result was an agreement that received a lukewarm reception. The Business Council on National Issues declared its support for the Agreement but noted that “the failure to achieve a barrier-free federation is due in large measure to protectionism, to political and bureaucratic turf struggles and to a genuine lack of understanding in some provincial quarters of the real costs of these impediments” (Wallace, 1994). Privately, Chief Negotiators agreed. According to Bob Knox, “[the following] was produced by Alan Barber [of MB] in the heat of negotiations in July. He probably would like to withdraw it now, but we shouldn’t give him the chance. I am sure he

⁵⁵⁰ Archives of Ontario, Folder B705175 – CMIT Meeting-June 27-28/94, “List of Future Negotiations,” 21 June 1994, p.5.

would appreciate (or deserve) any critical comments or catcalls you would care to offer”.⁵⁵¹ And thus Canadians may enjoy a condensed version of the “Ode to Internal Trade (Attributed to Alan Barber but not necessarily acknowledged):

The Agreement begins with a tiny preamble
Which according to some
Shows that signing is a gamble

Then operating principles, laudatory ambitions
Untouched by officials
Who prefer strong positions

The base for it all, the general rules
Not used anymore
Except by some fools

A procurement chapter, the agreement’s jewel
Except crown corps.
Where we still can be cruel
...

Plug your nose, free traders
For the chapter on booze
We’ve firmly entrenched
The land of the scmooze

Provinces love their natural resources
Don’t challenge them now
They’re on their courses

Energy proves to be ‘oh so’ elusive
All due to wheeling
Where talks were inconclusive
...

Transportation, all measures ‘listed’
We can’t touch those
We’re just too loose-fitted

⁵⁵¹ Archives of Ontario, Folder B705175 – Meeting: Chief Negotiators Sept 7-8/94, “Note to Chief Negotiators from Knox,” 15 September 1994, p.1-3.

Finally a chapter for those who are green
To rule above all else
And free traders too keen

A Committee of Ministers
To watch over it all
And make sure their 'x'
Is where the Secretariat will fall

On disputes, we'll leave these to a panel of lawyers
Chose with care, to ensure that we end up much poorer

And chapter 18, that hodge-podge of provisions
Where we all try to find
Our needed omissions

Add it all up, and I think that you'll surmise
It's the most Canadian of things
An 'OK' compromise".

Conclusion

The mandate to conduct negotiations, the completed AIT as signed on 18 July 1994, and the effort afterwards to update, amend, and expand it all suggest that the AIT was a window of opportunity for HoG summit institutionalization. An effort at microeconomic reform engaged the mechanism of continuous negotiation – first between HoG and then at ministerial councils. Within the mechanism is the potential to expand negotiations to include changes to intergovernmental decision-making. In Australia, a very similar process produced an institutionalized HoG meeting known as COAG. The process as it occurred in Canada resulted in a dead end for institutional reform, a conclusion that also applies in some respect to further economic reforms. In sum, the mechanism of continuous negotiation could not withstand an incentive to compete emanating from the political economy.

The AIT is “a complex and technically diverse intergovernmental agreement, attempting to deal with an ambitious range of issues affecting the integrity of the Canadian economic union” (Knox, 1998, p. 138). Its complexity lies in the multitude of exemptions to the general rule of mutual recognition.⁵⁵² Exemptions are allowed if proposed measures pursue a legitimate objective, are not more trade restrictive than is necessary to achieve said objective, do not unduly impair trade, and are not disguised trade restrictions.⁵⁵³ The Canadian Chamber of Commerce (1996, p. 16) was quick to criticize the AIT for its “lukewarm language...in committing governments to internal trade liberalization” along with its numerous “loopholes [particularly]...a blanket exemption for measures aimed at regional economic development”.

The optimistic view of the AIT is that it dealt with economic issues without compromising provincial policy capacity and provided governments with an agenda and general rules to structure future reform efforts (Knox, 1998). D. Brown (2002, p. 172) believes the AIT was “a significant achievement of Canadian federalism...[It] dealt comprehensively...with the remaining requirements for negative and positive integration...[and] fills the gap...in the original terms of the Canadian economic union”.

On the pessimistic side, “the most charitable appraisal that can be made is that the agreement constitutes a framework and a beginning for a genuine effort to remove provincial trade barriers”; it is a political document that “involves a great deal of bad or meaningless law” and grants the provinces the appearance of completely sovereign entities. (Mestral, 1995, pp.

⁵⁵² “Each Party shall accord to goods of any other Party treatment no less favourable than the best treatment it accords to: a) its own like, directly competitive or substitutable goods; and b) like, directly competitive or substitutable goods of any other Party or non-Party.” AIT Article 401 (1), Internal Trade Secretariat (2015). Similar language is used to refer to persons, services, and investments (see Article 401[2]).

⁵⁵³ Ibid., Article 404.

95-96). An Industry Canada communications brief stated that “the complexity of the AIT document may inhibit its application for many businesses...[It] is also complex in-so-far as it is a ‘process’ and is basically incomplete”.⁵⁵⁴

The pessimistic analyses regard the AIT negotiations as a political process that encountered serious difficulties. Parties failed to reach agreement on broad economic reforms, including mutual negotiation. Instead they managed only to tinker with some inefficiencies due to the presence of exemptions to the general rule. The result was that internal barriers became “the biggest solvable economic problem that Canadian politicians cannot bring themselves to solve” (The Canadian Chamber of Commerce, 1996, p. 17).

Allowing exemptions to the general rule was a direct result of the negotiations focusing on the issue of trade barriers rather than on issues of regulation. Discussing regulatory issues could have focused negotiators on harmonization and provincial sovereignty rather than on trade efficiency and mutual recognition. D. Brown (2002) states that the exemptions were a result of Canada’s focus on free trade rather than competition, whereas Australia focused first on competitiveness. Yet Canada did consider a policy of mutual recognition to deal with internal barriers. The question is why the same solution to the same set of economic problems was acted upon in one but not the other?

Mutual recognition’s adoption in Canada failed because provinces sought to curtail its application with the exemptions contained in each of the AIT’s sectoral chapters. As Schwanen (1998, p. 175) states, “the very idea of sectoral exceptions opens the door to serious gaps between the general rules and their practical application”. Bridging the gap depended on “how

⁵⁵⁴ Ottawa, COP.CA.2.2000-994, “External communications strategy for the AIT,” March 1996, p.5

well the parties come to grips with the theoretical tension underlying the agreement – the tension between the twin goals of economic integration and respect for diversity” (Lenihan, 1995, p. 112).

A significant aspect of the tension was the issue of regional development, with partisanship and a lack of leadership further curtailing the economic reform effort and the process of institutionalizing FMCs. Rather than be sold on the merits of national reforms, many of the parties involved were concerned about potential losses or their own ideological stances. Any restrictions on regional development – particularly on market access, government procurement, and Crown corporations – proved too politically sensitive. Actor’s responded by limiting and at times withdrawing their commitment to a comprehensive agreement; they continued to compete and argue for exemptions rather than seek cooperative solutions and infuse IGR institutions with significant value. In the end, an enduring conflict between industrial development and regional development may exist, where the former favours specialization and free trade and the latter seeks economic diversification via protectionism (Gilpin, 1972). The AIT remained embroiled in the latter issue and could not provide a bridge to the former. Its attempt to restrict the ability of provincial governments to pursue regional development was an unacceptable curtailment of their economic jurisdiction. The relative safety of concentrated external market integration allowed provinces to continue competing as they clung to their regional development and province-building policies. Whereas Australian states were confronted with the risk of the ‘turn to Asia’, Canadian governments faced no such risk.

When Ottawa refused to link economic reform with fiscal federalism, the sense of urgency that emerged to address Canada’s economic problems evaporated. Without urgency or risk, HoG

engagement and leadership was severely lacking. And without HoG using their authority to make political decisions and craft package deals, a decentralized negotiating process was established, which left the task of reform up to ministerial councils (D. Brown, 2002) and allowed competitive behaviour to reign. “[The ministerial committees] have the same problem of motivation, resources, and consensus as internal trade ministers and their officials” (Knox, 1998, p. 159). As such, this process managed only to cobble together an agreement riddled with loopholes and which lacked the benefit of general rules like mutual recognition. In Australia, mutual recognition became the default policy, requiring Australian governments to continuously negotiate on regulations. The implications of this particular form of microeconomic reform and of the fiscal reform negotiations led actors to found COAG. Australia’s goal of a more competitive and efficient economy to manage the ‘turn to Asia’ was incompatible with regional development policies that maintained domestic economic inefficiencies, which includes wide variation in accepted standards based on exemptions to the general rule. Yet in Canada this is exactly what occurred: “reciprocal non-discrimination does not even exist *within* the Agreement. More importantly,...the use of a very strong set of legitimate objectives in all chapters results in a wide range of exceptions to the intended philosophy of the Agreement” (MacDonald, 2002, p. 143; emphasis in original.).

The AIT negotiations were directly impacted by the political economy of Canada and the provinces. The various provincial viewpoints on the AIT “reflect underlying regional conflict of interest and deep-seated disagreement over the normative goals of the Canadian economic union...[resulting] in a less than ideal AIT and in its less than effective implementation” (D. Brown, 2002, p. 151). Different political interests were present in each sector, each sector was differently

exposed to the international market, and sector negotiators opposed national reforms, especially harmonization (Doern & MacDonald, 1999, p. 160). Officials familiar with internal trade have since commented on the lack of intergovernmental policy capacity. The lack of such capacity is one reason why the AIT “suffers from the disparate interests it tries to accommodate across governments” (Inwood et al., 2011, p. 239) Some governments eventually chose to complete bilateral deals, most notably the Trade, Investment and Labour Mobility Agreement (TILMA) between Alberta and BC, which has since been upgraded to include Saskatchewan under the New West Partnership Trade Agreement.⁵⁵⁵ As well, the AIT was politicized by ideological battles over free trade, whereas in Australia all parties eventually accepted and embraced the reform programme. Finally, as one FOI coordinator remarked, “when I ask internal trade officials about the AIT, they act rather sheepishly for not having completed the deal”.⁵⁵⁶

Having succumbed to the incentives of each provinces’ particular political economy, governments created a decentralized negotiating process that lacked a whole-of-government approach and allowed actors to seek protectionist exemptions. The mechanism of continuous negotiation managed to achieve some reform of the economic union and even managed to briefly expand the negotiations to include institutional reform. Actually establishing the linkage between economic and institutional reform was thwarted by a lack of HoG engagement and disagreements over economic reform. Canadian FMCs remained weakly institutionalized; they are not routinized and are not infused with much value.

⁵⁵⁵ Macmillan and Grady (2007).

⁵⁵⁶ Phone conversation with author, 18 June 2015.

The AIT process, like the SPC process in Australia, began with the potential to radically alter governance without the need for constitutional amendment. Indeed, it is an example of 'quiet constitutionalism', whereby constitutional change is produced without directly utilizing the amending procedures (McBride, 2003). According to Leeson (2000), it is not guaranteed that voluntary arrangements will fail in the face of self-interest. Rather it was entirely possible that "the [AIT] is likely to have an important impact on Canadian law and government policy. Most of its effects will come because governments feel an obligation to comply, whether or not they have the legal ability to do otherwise" (Swinton, 1995, p. 209).

In retrospect, the agreement is regarded not for its merits, economic gains, nor for its decision-making style. Leeson's (2000, p.18) observation that the AIT is "an entirely new way of approaching the role of governments at all levels in society" holds little water today. Rather the AIT was a success merely because an agreement was reached between all parties without any major conflicts, a huge accomplishment when compared to the era of mega-constitutional politics (Papillon & Simeon, 2004, p. 124). According to MacDonald (2002), the AIT is actually quite representative of Canadian federalism, which has always sought a balance between economic competition and political cooperation.

A best effort at economic reform did not lead to the significant reform of Canada's IGR decision-making process in order to ensure the reform effort's success. It was enough to just reach some kind of agreement. Brown conjectures that "this is understandable given the context of the recent failure at constitutional reform" (D. Brown, 2002, p. 177). But the Australian case demonstrates it is possible to leverage economic negotiations to achieve institutional change. Canada did not follow Australia, as the above process tracing has revealed. The next chapter, the

conclusion, completes the case study comparison and outlines its revelations about the future of both countries.

PART FOUR:

CONCLUSION

Chapter 7

[T]here is here [in Canada] no other family than the human family, whatever the language we speak, [whatever] the altar before which we kneel. Every day we rediscover the happy effects of this sacred work.⁵⁵⁷

Sir Henri Charles Wilfrid Laurier
Prime Minister of Canada, 1896-1911

[T]he colonies united will have a power they can only obtain by federation, and that power alone will give them a proper place in the family of nations. I ask you then, with unreserved feeling, with true hearts, earnestly engaged in this great work to drink this toast: One people. One destiny.⁵⁵⁸

Sir Henry Parkes
Premier of the Colony of New South Wales, various terms between 1872 and 1891

⁵⁵⁷ Valedictory address, McGill University Graduation Ceremony – Law, Montreal, 3-4 May 1864. Retrieved from <http://www.pco-bcp.gc.ca/aia/index.asp?lang=eng&page=key-cle>.

⁵⁵⁸ Banquet toast marking the opening of the Australasian Federal Convention, Sydney, 2 March 1891. Retrieved from <https://parkesfoundation.org.au/resources/sir-henry-parkes-2/in-his-own-words/>.

Australia and Canada are a fascinating example of a natural social science experiment, with many overlapping independent variables and – in the case of their HoG meetings – a divergent outcome measurable over time. Why did two similar political systems produce different outcomes regarding their institutionalization of HoG summits, such that Australia's COAG is a more institutionalized meeting at the apex of its IGR system whereas Canadian FMCs remain weakly institutionalized and disconnected from the rest of the system? This dissertation has sought an answer by process tracing two efforts at microeconomic reform, one that produced IGR institutional change and one that did not. There are many factors that led similar reform efforts to produce different outcomes, which the following conclusion elucidates as clearly as possible given the complexity of the comparison. It begins by examining the assumptions that comprise the theory of HoG summit institutionalization.

The process of IGR institutional change via economic reform begins when global economic shifts impact the economy. In both Australia and Canada, the 1980s and 1990s proved to be transformative. For Australia, lagging competitiveness vis-à-vis rapidly-growing Asian Tiger economies, current account deficits, internal trade barriers, and the 1990-91 recession combined to create a sense of economic crisis. Keating's 'banana republic' quip highlighted the major problems and suggested their solution: internationalize and liberalize the Australian economy via macro- and micro-economic reforms. The Commonwealth's initial effort at reform eventually required state participation since they retain sovereign powers over aspects of economic policy. The crisis's urgency, the proposed solutions, and the necessity of an intergovernmental response opened a window of opportunity for IGR institutional change.

The critical juncture that moved actors towards buying into a bona fide reform process was the spectacular failure of the 1990 Premiers' Conference. Competitive federalism between Canberra and the states hit a new low, risking the reform programme and Australia's prosperity. The risk associated with the status quo in the face of the 'turn to Asia' was too great, which caused PM Bob Hawke to launch the Special Premiers' Conference process. His speech and the Premiers' response to it engaged the mechanism of continuous negotiation.

In Canada, rising deficits, falling productivity, and adjusting to USA free trade were all significant problems that demanded reforms to the economic union. Canada's economic crisis was felt first at the provincial level, with several provinces grappling with recession and deficits early in the 1990s. Ottawa had spent the 1980s calling for microeconomic reform and also racking up its debt yet constitutional reform and Canada-USA free trade were the priorities. PM Brian Mulroney convened FMMs on the Economy in late-1991 and early-1992 to discuss and decide on issues of competitiveness and productivity, all within the context of the Charlottetown negotiations. Then, during PM Kim Campbell's brief time in office, microeconomic reform and a new federal-provincial relationship were offered, which helped sustain negotiations on whether to pursue an agreement on internal trade. PM Chretien's first FMM renewed the negotiation's mandate after a change of government, propelling the mechanism of continuous negotiation. The result was a window of opportunity for IGR institutional reform.

The examination of the crisis context of both cases demonstrates that both countries found themselves vulnerable to shifting world economic conditions. Saddled with long-term economic problems, both countries framed their economic crises in similar ways and proffered

similar solutions: a programme of liberalization and internationalization that included microeconomic reform through intergovernmental negotiations.

According to the theory of HoG summit institutionalization, convening a HoG summit to discuss a programme of reform engages the mechanism of continuous negotiation. From this point, Canada and Australia begin to diverge. In Australia, the mechanism was engaged at the level of the HoG via the SPC process, which convened over the course of the early-1990s to sustain a commitment to economic reform. The urgency of Australia's economic crisis and the risk inherent in its increasingly diffuse external market integration combined to incentivize cooperation. Having engaged the mechanism of continuous negotiations, actors committed to their cooperative reform process. As they achieved progress on economic reforms, they began to contemplate the institutionalization of the reform process's main institution, the SPC summits.

The mechanism of continuous negotiation expanded to include institutional reform because actors responded to incentives from the political economy. The option to maintain competitive federalism and retain as much policy manoeuvrability as possible – in order to compete for access to and investment from Asia – was overshadowed by the urgency and risk inherent in Australia's political economy at the time. Competitive federalism had proved too cumbersome and politically unstable to effectively manage both the 'turn to Asia' and the economic crisis. Increasingly finding itself without a stable and secure trading base, Australian leaders turned to each other to find solutions that eventually altered the characteristics of their federal political system.

The Canadian political economy was sufficiently different to produce a different outcome within a reasonably similar context. When the mechanism of continuous negotiation was

engaged, the political economy and political environment combined to relegate the mechanism to the level of Ministers. Microeconomic reform negotiations were decentralized to the various ministerial councils rather than encased in a whole-of-government approach within central agencies. They also remained technical in nature rather than strategic. HoG engagement was minimal even when negotiators were overwhelmed by skepticism and the debate on the agreement's comprehensiveness. The product of this debate was negotiations on only eleven sectors that focused on technical adjustments rather than strategic, long-term decision-making. The best face that John Manley could put on the AIT at the time was that it opened the door to further rounds of negotiations that may one day lead to real, comprehensive reform.

Contrast this to Australia, where HoG discussed a wide-range of issues, which demanded a whole-of-government approach from central agencies. Fiscal issues, social programs, and microeconomic reforms were all negotiated by HoG during the SPC process. Their ability to make political choices and reach package deals across various issues resulted in a successful reform process that expanded to include IGR institutional reform.

As in Australia, the structure of the microeconomic negotiations and the negotiations themselves were impacted on by the political economy. Provincial economic specialization and dependence on USA trade incentivized actors to compete with each other to secure access to the American market. It also incentivized an adherence to regional development policies and overall policy independence. An example is New Brunswick's effort to attract UPS's investment in call centres less than a year after the AIT was signed. Seeking economic development and diversification, it enticed American investment using its policy capabilities – on taxes, labour, and environmental standards – with little concern for the national economy as a whole or the AIT's

attempt to prevent provinces from unfairly using subsidies or regulations to undercut other provinces.⁵⁵⁹ It was an issue on which the CMIT could only agree to disagree despite its mandate to define internal trade rules.⁵⁶⁰

The New Brunswick example demonstrates that provinces are partly responsible for preventing the emergence of a wide-ranging reform programme at the HoG level. The other party responsible was Ottawa, which prevented the linkage of fiscal and economic issues. The federal government did not display the urgency or signal the same level of commitment as its Australian counterpart, and therefore sought to deal with each issue separately. Despite the efforts of Ontario Premier Rae and others to include fiscal federalism, it was not a topic up for discussion. The lack of urgency was also felt by the provinces, who only reluctantly engaged on the internal trade issue; they questioned the existence of internal trade barriers and the amount of money to be saved and they balked at any curtailment of their regional development powers. Without a broader reform programme, the security offered by the FTA caused provinces to continue competing and thus to resist any curtailment of their economic powers. A neutral chair and Ottawa acting as just another partner in the negotiations were not enough to convince the provinces to jointly and cooperatively level the playing field with regard to the exercise of their sovereign economic powers.

The archive data demonstrates that provincial actors were preoccupied with the unique needs of their own economies and their abilities to fully exercise their sovereign powers in order

⁵⁵⁹ Archives of Ontario, Folder B705175 – CMIT Meeting April 11-12/95, “Background Note: Labour Standards and Investment Attraction,” 6 April 1995, p.1.

⁵⁶⁰ Archives of Ontario, Folder B705175 – CMIT Meeting April 11-12/95, “CMIT Calgary: Meeting Scenario Note,” 7 April 1995, p.8; see also same folder “News clipping: UPS move probed,” 13 April 1995.

to achieve the goal of economic development. BC focused on the Pacific and Saskatchewan on its Crown corporations. Ontario and Québec sought to maintain their powers of economic intervention even as they recognized the distorting effects of internal barriers, which did ultimately bring them, and their feuds over wine and construction workers, to the table. The Atlantic Provinces were content to act independently – as New Brunswick did with UPS – secure in the knowledge that regional development programmes remained largely exempt from internal trade rules. Even dismantling some relatively minor trade barriers and establishing the ITS to oversee the process were viewed as too high a price to pay given the alternative of individually managing their economies; competition remained the preferred option rather than cooperation. Several former senior government officials confirmed that the political costs of internal trade reform far exceeded the purported benefits in terms of savings for businesses and consumers. They stated that after the Charlottetown Accord's defeat, few politicians were willing to take extreme risks. Bob Rae, one of the key architects of the Accord, is perhaps a notable exception and his single term in office highlights the risk inherent in the political impetus provided by HoG: they take chances at their own risk.

In short, none of Canada's major players bought-in to the reform process even though they conceded that Canada's economy was in crisis. Whilst some were ideologically opposed to free trade, the major impediment was that Ontario, BC, and Québec did not fully buy-in to the process in the same way as their Australian counterparts. Québec's interventionist style of economic management and BC's focus on the Pacific are but two examples of how each province saw a domestic reform programme not through a lens of national action but through their own unique lenses of economic development. Secure in their access to the American market,

provinces were confronted with little incentive to risk a national reform process that could diminish their power and influence. The counter example from Australia is Victoria. Even though Premier John Cain initially opposed the liberalization programme in favour of his own policy of government intervention, he eventually acquiesced.

Protectionism, regional economic specialization, and government intervention are present in the economic histories of both Canada and Australia. According to a former provincial trade official, “the remnants of [the National] policy have locked in many provincial policy choices”.⁵⁶¹ In Australia, the scale of the economic crisis – its perceived urgency and the risk of the ‘turn to Asia’ – convinced leaders to overturn their entrenched policies and embrace cooperative, national reforms. Rather than the southern manufacturing states aligning against the resource-rich states, they all recognized that their individual goals were reflected in a concerted domestic reform programme. All of Asia was beckoning and the only way to take advantage was to cooperatively manage economic reform. Australia had no dominant buyer of its exports and no safe harbour for its economy, which produced a situation that helped Australian leaders accept the risk of cooperation.

In Canada, an economic crisis also existed but its external trade structure did not generate concerted national action. Canada has a dominant buyer of its goods and no shift was occurring. The USA, especially with the free trade agreement in operation, is generally a safe harbour, which is a situation that produces incentives adverse to cooperation. Even though some of the smaller players were enthusiastic AIT supporters (especially AB and MB), the fact that the major sub-units – BC, Ontario, and Québec – remained skeptical severely impacted the ability of the

⁵⁶¹ Interview, 11 August 2015.

mechanism to function. The urgency of the problem was not acted upon by all parties and the incentive for national cooperation was outweighed by the incentive to compete.

The turn from competition to cooperation in Australia was also helped by the genuine commitment offered by Hawke and the level of support and credibility that NSW Premier Nick Greiner brought to the reform programme. It also helped that some of the other smaller states, such as SA under John Bannon and QLD under Wayne Goss, were enthusiastic supporters of reform. This points to another variable that was critical to the process of institutionalizing HoG summits: leadership. Whereas champions of reform were present in Australia to help propel the reform process, leadership was sorely lacking in Canada to the extent that the incentive to compete from the political economy proved insurmountable. The Canadian and Australian cases thus demonstrate that vision and leadership were all the more critical to the process of institutionalization.

Whilst champions of reform were present in both Canada and Australia, it matters who those leaders were. In Australia, Hawke made economic reform a central plank of his last election campaign and he was genuinely ready to reform fiscal federalism and IGR. He made many speeches in which the very future of Australia was bound up with his reform agenda. His profound vision for Australia and his relationship with the people deep into his tenure were enough to lead him and the Premiers down a new avenue of reform. It was risky, and Hawke eventually lost his job as PM because of the lengths he was willing to take to reach a grand bargain with the Premiers. Indeed, most of the Premiers involved in the original SPC process also did not survive for long in government (for reasons not directly tied to the SPC process). Lawrence and Cain were defeated at the polls due to slumping economies after long years in government whilst

Bannon and Greiner resigned because of perceived mismanagement. These incidents were not enough to derail the reform process, and the succeeding Premiers and PM were able to found COAG.

In Canada, some within business, government and the bureaucracy – particularly Bob Knox, Arthur Mauro, and John Manley – recognized the need for reform but a champion of reform in the right place never really emerged. Reforming the economic union remained a technical and bureaucratic endeavor. Except for brief moments of political saliency at FMMs in 1991, 1992, and 1993, the issue rarely reached the HoG level. No HoG involvement meant no opportunity to realize that working together to reform multiple policy areas is effective and should continue. Kim Campbell, like Bob Hawke, had seen the light, but like so many other long-lived governments, the Progressive Conservative's time was up. For her successor Jean Chrétien,

idealism was never part of the scrapper's makeup. Politics was not about the pursuit of noble ideals or the realization of high ambitions for the country. It was about the fighting man getting his way. His best moments, Chrétien would say, came not with the passage of legislation but with election-night triumphs (L. Martin, 2003, p. 72).

How fascinating that Chrétien and Hawke, both from a labour background, had such different styles when in office. Hawke too was a fighter, but his desire for conciliation and vision for Australia starkly contrasts with Chrétien's "terrible impatience for detail and he showed few signs of being able to understand...the great currents of change, both the dismal and the grand, sweeping the world around him" (L. Martin, 1995, p. 376). It is likely Chrétien endured one too many battles against nationalists in Québec and province-builders elsewhere for him to commit personally to the reform process. A lack of urgency and risk also contributed to Ottawa's

unwillingness to simultaneously offer a closer partnership with the provinces on internal trade, fiscal reform, *and* IGR institutional change.

Chrétien's leadership or lack thereof is not solely to blame. Every Premier was largely concerned with their own affairs. Regarding the major actors, Bob Rae and Daniel Johnson were more concerned with their own issues and solutions in the face of recession and perceived mismanagement (and even the risk of separation). Klein, champion of free trade, never achieved the national standing amongst his peers that Bannon – also Premier of a smaller state – used to convince the reform laggards. And Harcourt stated clearly in his memoir that his days as 'Captain Canada' were over after Charlottetown. Indeed, Charlottetown is a factor that cannot be ignored. HoG at the time of the Charlottetown referendum were extraordinary for taking a huge political risk but, according to a former senior official, "after Charlottetown, there was no momentum to reform".⁵⁶² Only Campbell floated the idea of re-engaging on some of the non-constitutional issues – such as fiscal federalism and economic reform. Whether or not she was offering a genuine proposal akin to Hawke's 'closer partnership' is a counterfactual for a different paper. In the end, mega-constitutional politics exhausted Canadian leadership. Without it, institutionalizing HoG summits became much more difficult. Canada's concentrated external market integration and its regional development needs prevented the mechanism from expanding negotiations to include institutional reform. Without leadership, the political economy incentive to compete proved insurmountable, thereby closing shut the window of opportunity to institutionalize FMCs.

⁵⁶² Interview with former senior provincial government official, 26 August 2015.

The significance of leadership is implied in the theory of HoG summit institutionalization – when it describes the major players ‘buying-in’ to the reform process – but it was not fully elaborated in the theory chapter. Both cases help correct this and point to leadership as a key factor in how the mechanism of continuous negotiation operates. According to Hale (2004), IGR effectiveness and, in this case, change depends on the willingness of governments to acknowledge shared political and economic interests. Without direct political impetus from HoG, and within a context of concentrated external market integration, continuous negotiation on economic reform never spilled over into IGR reform. The mechanism is therefore not an automatic process that leads to institutional change. It is conditioned by several factors, which this study has demonstrated must also include leadership and political economy.

The dissertation contributes to the literature by more concretely adding political economy to the list of factors impacting HoG summits and IGR system. The alternative explanations, including partisanship, personality, political parties, elections, and fiscal federalism, have been used to explain HoG summit institutionalization (or lack thereof). The above narrative acknowledged these factors as important but not sufficient to offer a compelling explanation for the observed outcomes and their timing.

The comparison of Canada and Australia confirms to an extent Esselment’s research that the process of negotiating intergovernmental agreements and their implementation are impacted by partisan considerations. Partisanship is part of the reason for provincial governments’ attitude towards the AIT. Yet the story remains incomplete; partisanship is present but the political economy incentive also impacted the AIT.

Partisanship and party system are variables that emerged in both the Canadian and Australian narrative. Overall, left-leaning governments were far more skeptical of free trade and internationalization than right-leaning governments. State governments under Labor were at first skeptical of the Commonwealth's neo-liberal reforms, mirroring their NDP counterparts, whereas Liberal-governed states and Progressive Conservative-provinces embraced these reforms. Thus, partisanship places actors at the starting line of a reform process. As the process unfolds, the party system variable is only part of the explanation for the different outcomes. In Australia, a more integrated party system is the purported reason why Labor state governments became amenable to reform, since Labor also governed the Commonwealth. Whereas in Canada, a more disintegrated party system seems to explain the intransigence of some provinces towards Ottawa's reforms (and the enthusiasm of others).

Whilst accurate, the partisanship and party system variable do not fully account for the observed outcome. The reforms in Australia were proposed by a Labor government and supported by both Liberal and Labor state governments. The opposition from Labor governments was overcome not only because of party linkages but also because of economic circumstances that shifted the governing party's position over time. As well, the partisanship and party system variables do not account for the timing of the shift from competitive to cooperative IGR in Australia. The 1990 Premiers' Conference was dominated by Labor governments yet it produced a most uncooperative outcome. As well, Hawke's biggest supporter was Greiner, a Liberal Premier. His support should not have been forthcoming if partisanship and party system are the only variables that explain the SPC process and founding of COAG. As McClintock (2013, p. 72) recognized, political harmonization is not necessary to achieve reforms. Completing the story of

COAG and understanding the moments that transcend partisanship and party system require the inclusion of the political economy.

The same is true for the Canadian case. Even though partisanship and party system may offer stronger explanations than in the Australian case, ultimately they cannot solely explain the AIT's outcome of weakly institutionalized FMCs. Ottawa's reform plan remained constant despite a change of governing party. And whilst provinces' positions aligned with the partisan leanings of their governing party, these positions changed over time to produce an agreement, albeit a weak one. Ontario's position changed the most radically, from opposition to free trade both domestic and international to accepting an internal trade agreement based on the economic benefits of lower trade barriers in areas such as government procurement and on new rules governing provinces' ability to enact regional development policies.

As well, the idea that the presence of Québec automatically skews Canada toward less cooperative outcomes than Australia must be viewed cautiously. Québec's position during the negotiations is remarkably similar to the other NDP provinces' desire to retain policy interdependence and regional development powers. Québec is categorized as a pragmatist because the provincial Liberal Party is ideologically more open to free trade but ultimately Québec's political economy helped to condition the partisanship and demographic variables, thereby providing a more complete explanation of its behaviour during the AIT negotiations. In the end, Québec acted in its economic interest just like the other provinces.

Another alternative explanation that is present in each case study is fiscal federalism. Ottawa was determined not to cede away its spending power and so avoided cooperatively addressing fiscal federalism in a multi-lateral forum. The federal budget situation also prevented

Ottawa from spending on reform programs, which was probably required to reach a fully comprehensive, multi-policy deal with the provinces.⁵⁶³ In Australia, the Commonwealth faced similar pressures regarding its budget deficit and spending power. Yet Hawke committed to examining the fiscal issue with the states, a direct result of the 1990 Premiers' Conference dustup. In Canada, Bob Rae's emergence as a powerful voice advocating for fiscal reform found no counterpart in Ottawa to champion such reform. In the end, David Dodge and Paul Keating performed very similar roles in their respective countries. It is the timing of their actions that is crucial. Whereas Dodge and most likely Paul Martin prevented the linkage of economic and fiscal issues, Keating's involvement occurred well after the process of reform had begun. Eventually, Keating did manage to prevent full-scale reform but was unable to stop the SPC process' momentum in other areas, particularly microeconomic and institutional reform.

The fiscal federalism issue demonstrates clearly that the federal government, a major player in any reform effort, must also fully buy-in to the broader reform programme. Whereas Hawke confronted the urgency of the economic crisis and 'turn to Asia' with a bold commitment to reform, the fact is the situation in Canada was not so urgent, allowing Ottawa to address the fiscal situation independently of its economic reform programme. The tighter fiscal relationship between Commonwealth and states helped to bring about the emergence of more cooperative federalism but the actual process of reform itself was engaged because of the risk inherent in Australia's changing political economy. Canada's fiscal federal system was equally in need of reform but the competitive incentive and lack of urgency kept Ottawa from committing to a broader reform programme.

⁵⁶³ Interview with former senior provincial government official, 26 August 2015.

The comparison of Canada to Australia adds to both the federalism and IGR literatures of both countries. In Australia, the role of leaders such as Hawke and Greiner was enriched by the mechanism of continuous negotiation. COAG is a product of their political vision and courage but leadership churn is not the only factor that institutionalizes cooperation. Their success was due in part to the incentives emanating from the political economy. The institutionalization process began when the Commonwealth enacted macro-economic reforms that directly exposed state economies and the IGR system to external pressures. The process continued when Canberra shifted to microeconomic reforms, which involved areas of state jurisdiction. With state economies and the IGR system buckling under the weight of reforms and external pressures, Hawke launched his 'closer partnership' agenda to meet his goal of transforming the Australian economy. What he and the other leaders achieved was reform through a series of negotiations that helped them to realize that IGR institutional change could secure implementation and sustain progress. Their realization demonstrates that leaders will have a greater chance of success if political reform is accompanied by meaningful economic reform cooperatively achieved. COAG became the counterbalance to the institutionalized conflict already inherent in Australian federalism.

In Canada, the study demonstrates the limits of the continuous negotiation mechanism as well as the significance of the political economy variable. Even with a process of economic reform engaged, the incentives to compete are themselves more institutionalized than they are in Australia. Canada's political economy did not undergo similar changes and did not produce a similar level of vulnerability such that it produced institutional change. Actors in Canada saw no reason to risk nor were presented with a compelling reason to cooperate.

Yet the AIT also demonstrates that cooperative results are achievable without formal cooperation; in other words, cooperation can emerge from competition hence why so many scholars and analysts mis-predicted that the AIT represented the dawn of a new, more effective method of policy-making. The AIT was not a total failure, its outcome was just the way the Canadian federation functions (a reality not lost on the AIT negotiators and their poem). It functions this way because of a major difference with Australia: concentrated external market integration, which fuels competitive federalism and weakens IGR. Instead of viewing this with melancholy, the Canadian federal system is innovative and flexible. In the face of international competition and USA dominance, the provinces and Ottawa are able to search for solutions via their own jurisdictional and spending powers; Canada is a remarkable example of federalism's potential to act as a policy laboratory.

The fact that the United States affects Canada is not new. Understanding just exactly how it does so is an ongoing endeavor. This particular study demonstrates that the USA directly affects Canadian IGR to an extent not fully realized in the Canadian literature. It also confirms, as does the Australian case, that globalization and external forces do indeed shape IGR systems. Canada's long reliance on USA trade has thus determined in part the nature of its IGR system, which also has endured over time, leading scholars to claim that it is unaffected by outside forces. In fact, the opposite is true, leading to a simple and profound conclusion: Canada will never have a formal system of IGR with institutionalized FMCs so long as it has one major trading partner. All the prior advocations for formality and routinization – and complaints of a lack thereof – are for naught. Nevertheless, cooperative solutions are capable of bubbling to the surface. And like any good bubble, it eventually pops. Canada's federal political system and political economy prevented the

mechanism of continuous negotiation from functioning as it did in Australia. This is not to say it can never function only that its ability to sustain and expand reform processes in the Canadian context is diminished. The key to overcoming the dual existence of competitive and collaborative federalism – referred to as the paradox of Canada’s federal condition – as well as the faltering of the mechanism is through leadership, which was not present to the same extent as it was in Australia.

There are glimmers of change however. As Canadian trade diversifies and economies rely less on the USA and more on China and other rapidly developing economies,⁵⁶⁴ the desire – and need – for provinces to work together may increasingly manifest on the national stage. Already Premiers are meeting regularly as the CoF and have requested many times to meet with their federal counterpart in order to make decisions.⁵⁶⁵ The CoF parallels the Premiers-only Adelaide summit that sustained the Australian reform effort despite the Commonwealths’ political turmoil and intransigence. The dissertation’s findings suggest that as Canadian trade diversifies – as the Trans-Pacific Partnership and EU free trade occupy a greater part of the trade dynamic – the need and desire to cooperate through IGR institutions will grow, thereby sustaining Trudeau’s renewed effort at intergovernmental engagement. Rather than compete for access to one trading partner, the provinces and Ottawa may cooperate to collectively improve the competitiveness of the Canadian economy in the face of a growing multitude of trade opportunities. And much like the Australian states learned to cooperate with each other to make national policy through the SPC

⁵⁶⁴ Canada’s share of exports declined from a high of 44.4% in 2000 to around 30% in the last four years, although whether this trend will continue long past the Great Recession and oil price slump is yet to be determined (World Bank, 2015b).

⁵⁶⁵ See 2006 Council of the Federation Advisory Council report. Retrieved from http://canadaspremiers.ca/phocadownload/publications/report_fiscalim_mar3106.pdf. The latest version of this report does not mention FMCs.

process, so too may Canadian provinces increase their multi-lateral effectiveness through the CoF.

Berdahl makes just that contention when she argues that institutions along with ideas are responsible for the provinces' renewed interest in internal trade policy. The idea of free internal trade has in fact existed for decades, it just needs the right institution to find expression. The dissertation has further postulated that the creation of institutions also emerges from ideas, which are expressed through the mechanism of continuous negotiation within a context of economic reform. Investigating the factors that led to the creation of the CoF is a next step to understanding the theory of HoG summit institutionalization in Canada.

Are Canadian governments prepared to collectively control the country's adaptation to changing world market conditions or will they disperse that power to individual governments to independently react to outside forces? Part of the answer is that the fault is in ourselves *and* in our stars – stars and stripes that is. At times there is just no resisting the pull of continentalism, even when the policy goal is the perfection of the Canadian economic union. Canada also suffers from a lack of national leadership; there are 11 or more hands on the wheel of the Canadian ship of state, most of them capable of acting independently. It is a ship without a bridge that could bring together all HoG to determine a common course. If Canada is to improve its capabilities to adapt to global economic changes, if Ottawa is to retain any power beyond the spending purse, and if the provinces are ever to transform their export dependent and single industry-reliant economies, then Canadian leaders are well-advised to follow their Australian counterparts and form a closer partnership.

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