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Tax Devolution and Intergovernmental

> We will implement the proposals of the Calman Commission and introduce a referendum on further Welsh devolution. (p28)
>
> We recognise the concerns expressed by the Holtham Commission on the system of devolution funding. However, at this time, the priority must be to reduce the deficit and therefore any change to the system must await the stabilisation of the public finances. (p28)

A central theme in this *Agreement* is maintaining the strength of the union during a period of financial crisis. A key element of their strategy is that 'The constituent parts of the union must have arrangements appropriate to their needs'[2]. Also important is ensuring elected representatives from the nations in the UK are accountable to their constituents for the decisions they make. Put differently, that which elected representatives vote for is that for which they are responsible. This latter issue lies at the heart of the West Lothian Question[3] which is focussed on 'ensuring that legislation on devolved issues that only affect England, or England and Wales, can only be passed with the consent of MPs from England, and where applicable Wales'[4].

For the new UK Government, the challenge is how to match the rhetoric on devolution in the *Agreement* with the substance of governing in an environment characterised by a sizeable national budget shortfall and large public sectD.cTf2.6066ebothia.14.ued Lhei

allocation model under funds Wales (by £400 million) and substantially over-funds Scotland (around £4 billion)[6].

The purpose of this paper is to draw on the Australian experience with funding its devolved (State) governments and what lessons the UK can learn from this experience as it moves towards greater devolution during a period of financial crisis. As background to this discussion, Section 2 provides an overview of the budgetary challenge currently confronting the UK and some of the funding options which might impact on and cause problems for DAs (and England) and the union.

Two options available to the UK Government to shift some of the financial burden of central government to regional governments ar

2. How big is the UK Budget Crisis?

With a collapsing economy and rising unemployment, the impact on the UK Government budget was rapid and dramatic. From a deficit equal to 0.4% of GDP in 2007-08, it was estimated in the June 2010 Budget to rise to 7.5% of GDP and not decline from this level until 2011-12 (Table 1). In 2009-10, this budget deficit is equivalent to twice the revenue from the VAT or almost as much as current personal income taxes. Put more simply, by the end of 2009-10, the UK was estimated to raise 25% less revenue than it needs to fund its spending. A direct result of these ongoing high budget deficits is a doubling in public sector net debt (PSND) from 36.5% of GDP in 2007-08 to an estimated 53.5% in 2009-10. Prior to the June 2010 Budget, PSND was forecast to be 74.5% of GDP by 2013-14. Even after the changes introduced in the June 2010 Budget, it was still forecast to be 70.3% (Table 1).

In responding to this budgetary crisis and the deteriorating economic position, the UK Government has been canvassing all possibilities. What Table 1 shows is that the actions taken by the new coalition Government in the emergency 2010 UK Budget (June 22) might have reduced government expenditure and increased taxes (such as raising the VAT rate from 17.5% to 20%), but that the Budget will not be balanced until 2015-16 and by then, PSND will be 67.4%, up from 35.5% in 2007-08.

TABLE 2: S

3. TAX ASSIGNMENT

Seven basic options are available to the UK Government in their dealings with Devolved Administrations (and England) if they are intent on exacting from them a greater contribution to reducing PSND:

1. change expenditure assignment;
2. change tax assignment;
3. encourage (or force) own-tax increases;
4. reduce general grants;
5. transition from general to specific grants;
6. change the method of distributing general grants; and
7. change the method of managing specific grants.

Since Federation in 1901 Australian States have experienced all seven options as a result of their changing and evolving relationship with the Australian Government. In fact, in the past two years alone, all options have found application and debate. On 1 January 2009, the Australian Government and States agreed on a new approach to allocating specific grants which involved introducing fewer specific grants (from over 90 to just 5 payments) accompanied by a greater focus on performance monitoring and the availability of reward payments for the achievement of agreed objectives (option 7). On 28 February 2010, the Commonwealth Grants Commission (CGC) introduced, wh.4(Attion

TABLE 3: SUMMARY OF EXPENDITURE ASSIGNMENT IN THE UK AND AUSTRALIA: 2008-09

How the UK and Australia go about funding their devolved governments is very different. Table 4 details tax assignment in the UK and Australia. In 2008-09, this saw the central government in Australia raise 82% of tax revenue, States 14.8% and local government 3.2%. In the UK, the comparable figures for 2007 were 94.8%, 0% and 4.7% respectively, with supra-natio

own economies because they have direct access to revenue from taxes levied on broad bases. What is critical though, is that States have some discretion over the taxation of their own base.

In the UK, the lack of any substantive tax assignment to DAs must be changed if there is to be any genuine move to further devolve government. The recent recommendation by the Calman Commission (2009, p111) to assign greater revenue raising powers to the Scottish Government through assigning 10p of the basic and upper personal income tax rates (with scope for additional imposts), is a positive move in this direction. So too is the Holtham Commission (2010, p72) recommendation for the revenue from 10p, 20p and 25p of the basic and higher rate bands (Table 5) to be assigned to the Welsh Government. However, there are important lessons to be learnt

TABLE 6: TOTAL TAXATION REVENUE 2008-09

	$m	%	$m	%	$m	%	$m	%
Taxes on income								
Income taxes levied on individuals								
Personal income tax	124,029	44.6%					124,029	36.6%
Fringe benefits tax	3,581	1.3%					3,581	1.1%
Total	127,610	45.9%					127,610	37.7%
Income taxes levied on enterprises								
Company income tax	62,784	22.6%					62,784	18.5%
Income tax paid by superannuation funds	9,201	3.3%					9,201	2.7%
Total	71,986	25.9%					71,986	21.2%
Income levied on non-residents								
Dividend withholding tax	303	0.1%					303	0.1%
Interest withholding tax	1,035	0.4%					1,035	0.3%
Other income taxes levied on non-residents	436	0.2%					436	0.1%
Total	1,774	0.6%					1,774	0.5%
Total	***201,369***	72.4%					***201,369***	59.4%
Taxes on employers payroll and labour force								
Employers payroll taxes			16,402	32.7%			16,402	4.8%
Other employers labour force taxes								
Superannuation guarantee charge	377	0.1%					377	0.1%
Total	***377***	0.1%	***16,402***	32.7%			***16,779***	5.0%
Taxes on property								
Taxes on immovable property								
Land taxes			5,565	11.1%			5,565	1.6%
Municipal rates			179	0.4%	10,758	100.0%	10,946	3.2%
Other			1,017	2.0%			1,017	0.3%
Total			6,761	13.5%	10,758	100.0%	17,519	5.2%
Taxes on financial and capital transactions								
Financial institutions transactions taxes								
Government borrowing guarantee levies	16	0.0%	386	0.8%			402	0.1%
Stamp duties on conveyances			9,534	19.0%			9,534	2.8%
Other stamp duties			304	0.6%			305	0.1%
Total			10,225	20.4%			10,225	3.0%
Total	***16***	0.0%	***16,986***	33.9%	***10,832***	100.7%	***27,834***	8.2%
Taxes on the provision of goods and services								
General taxes (sales taxes)	1,090	0.4%1,090.3w.610 1 T0din						

(akin to the base of the local government rates). In fact, the proposal does consider the scope for the State land tax to be administered by local government as part of their local government rates. The third major reform was to the taxation of transport related services and in particular, a move toward congestion charges and market based road pricing. At the same time, State Payroll Tax, property conveyancing duties and insurance and other stamp duties would be repealed, while gambling taxes would be reformed to ensure they are more uniform and capture rents.

While there is broad acceptance that the current tax assignment in the Australian federation is less than ideal (Freebairn 2010, W.154,7n0

In the case of Scotland, there currently exists an option for it to add an additional 3p to the basic rate of personal income tax paid by its residents. The recent Calman Commission (2009) proposal for the introduction of a Scottish Variable Rate (SVR) of income tax administered by HMRC has received UK Government support as a replacement for the current 3p option. With the Scottish Variable Rate of income tax, the default arrangement would be that 10p of the basic and higher rates of personal income tax paid by Scottish residents (Table 5) would be assigned directly to the .0003 Toed di

sharing options) or to reduce grants equivalent to any revenue raised from actions not sanctioned (as with the State own-tax on income in 1942).

TABLE 8: HENRY REVIEW RECOMMENDATIONS FOR REFORMING STATE TAXATION

Tax	*Short term*	*Medium term*	*Long term*
Payroll Tax	Base broadened through reducing/removing threshold.	Rate increased	Repealed
State Cash Flow Tax (or Business Activity Tax)			Introduction of Cash Flow Tax accompanies repeal of Payroll Tax and most stamp duties (other than conveyancing)
Insurance Duty	Repeal Fire Service Levy component	Repeal other insurance duties	
Other Stamp Duties	Progressive repeal (funded through changes to payroll taxation)		All repealed
Land Tax	Base broadened through reducing threshold;	Base broadened through removing exemptions; increase rate and reduce conveyancing duty	Rate increased and conveyancing duty repealed Local government administer land tax with Local Rates and Fire Service Levy
Property Conveyancing Duty		Reduce duty	Repealed
Gambling taxes	Set rates to recoup rents. Abolish concessions, an industry support through direct expenditures		
Road transport taxes (Progressive implementation)	Introduce congestion taxes and market based road pricing. Motor vehicle ownership and use set related to road provision. Government administration funded through user charges.		

Source: Henry Review (2010), Volumes 1 and 2, Warren (2010a)

While ever a DA does not impose its own-tax legislation and have its own tax administration, the risk will always be there that the UK Government may not be cooperative and could act to be unresponsive or positively antagonistic towards any proposed DA tax changes. This would be expected if such changes were seen as

In summary, there are three basic options available to sub-national governments intent on increasing their access to taxes and tax bases administered by a central government:

1. Share tax revenue;
2. Share tax bases;
   a. with harmonised base, own rate but central (or shared) administration of the State tax (eg 'Piggyback' Scottish Variable Rate personal income tax)
   b. with harmonised base, and own tax and administration of the State tax (eg reforms to local property tax base managed at national level but tax imposed at local level)
   c. with own tax base, rate and administration of the State tax (eg land tax at State and local level)
3. Reassign taxes
   a. central taxes assigned to sub-central governments (eg Payroll Tax in Australia assigned to States in 1971)
   b. sub-central taxes assigned to central government (eg the introduction of the Council Tax in 1991 effectively assigned the determination of the local property tax base to the UK central government and rate setting to DAs in consultation with the UK government)

What the Australian experience has shown is that revenue sharing (1 above) without a legally binding agreement between the levels of government sharing the tax is prone to failure. With no formal binding agreement, the government collecting the revenue can arbitrarily rescind the arrangement, impose reforms to this tax which directly impact the level of revenue being shared, or more fundamentally, arbitrarily change the proportion of the revenue being shared.

Reassigning minor tax bases to sub-central governments (3 above) is also not a long term solution and potentially the source of economic inefficiencies (as the Henry Review (2010) concluded in relation to the current Australian State Payroll Tax). However, such minor taxes (and own-income taxes) might have a role in ensuring accountability by DAs who confront 'hard budget constraints' (as in Scotland and Wales) such that a direct link can be drawn between increased expenditure and increased funding. In Australia, soft budget constraints and substantial VFG has done little to encourage accountability by States. For DAs, access to own-taxes on broad bases is essential. While the Calman and Holtham Commissions proposed these taxes being linked directly to the UK income tax, there is a strong case for the DAs imposing their own legislation related to such a tax.

None of the discussion in this section has considered the important issue of how any new taxes in DAs will impact on their grant allocation in the longer term. While both the Calman and Holtham Commissions supported a full offset against grants to DAs for the basic rate structure in Table 5 and some tax reassignment, the important question is how might the UK government then respond in an attempt to shift some of the burden of addressing its current budgetary crisis to DAs through changes to grants. To this end, we need to review how current intergovernmental transfer arrangements might change following any tax reassignment and how this might impact on both the quantum and distribution of grants amongst DAs and England.

4. INTERGOVERNMENTAL TRANSFER ARRANGEMENTS

In theory, there is no reason why the financial obligations accompanying any expenditure assignment should ultimately equate to the revenue arising from any tax assignment. For reasons of equity, efficiency and simplicity, some level of intergovernmental fiscal transfers is justified. Principal amongst these reasons are:

1. the achievement of national priorities (and so the need to override local preferences);
2. positive externalities (or spillovers) associated with State expenditure (and the resulting risk of under-expenditure by States);
3. negative externalities associated with State expenditure (such as congestion);
4. States have varying access to tax bases;
5. States confront differing disabilities (eg cost structures) in the delivery of services; and
6. economies of scale in delivery of services and the administration of taxes.

Even if these issues were not important, a *fiscal gap* may arise for a sub-central government because either the central government has greater revenue raising capacity (vertical fiscal gap or VFG)) or because comparable sub-central governments have a greater capacity to raise own-source revenue than similar governments (horizontal fiscal gap or HFG). In practice, these issues are resolved primarily through intergovernmental fiscal transfers between levels of government and through transfers being distributed to reflect tax capacity and expenditure disabilities.

Four elements typically characterised most intergovernmental transfer arrangements:

1. A grants management process which focuses on the form of the consultative and performance assessment framework;
2. Grant design issues including the mix of general and specific grants;
3. Grant value determination which could be based on some fixed formula (eg tax share) or variable arrangement (such as based on needs and priorities); and
4. General grant distribution arrangements which are based typically on fiscal equalisation principles.

Any push for further devolution in the UK inevitably raises the issue of the appropriateness of current intergovernmental transfer arrangements and how they, or any changes to them, might interact with changed tax and expenditure assignment. The Calman and Holtham Commissions recognised this issue but did not fully acknowledge its implications, in fact confusing two important issues in making their recommendations. On the one hand, they recommended a move away from current grant allocation arrangements towards applying fiscal equalisation principles; while on the other, recommending DAs have imputed to them a grant equivalent to the revenue collected from the income tax rates in Table 5 – even where these rates are different in practice. However, these tax assignment proposals are not compatible with rigorously applying fiscal equalisation principles when allocating grants amongst DAs.

The risk for the Calman and Holtham Commission proposals on intergovernmental transfer allocation is that they lack a systematic approach to the problem and that this

tax design in Australia and shows just how significant but little understood is the potential disincentive this interaction might be to any State either reforming current taxes or introducing new ones – an issue not even addressed in the recent Henry Review (2010) recommendations on State tax reform.

If the UK government moves to have DAs bear a greater share of the burden of addressing public sector net debt through reduced and redistributed grants (with or without tax and expenditure reassignment), it cannot achieve this simply with a focus on introducing fiscal equalisation principles (4 above). Rather, based on Australian experience, elements (1) through (4) must be addressed sequentially to ensure the approach taken avoids division and derision.

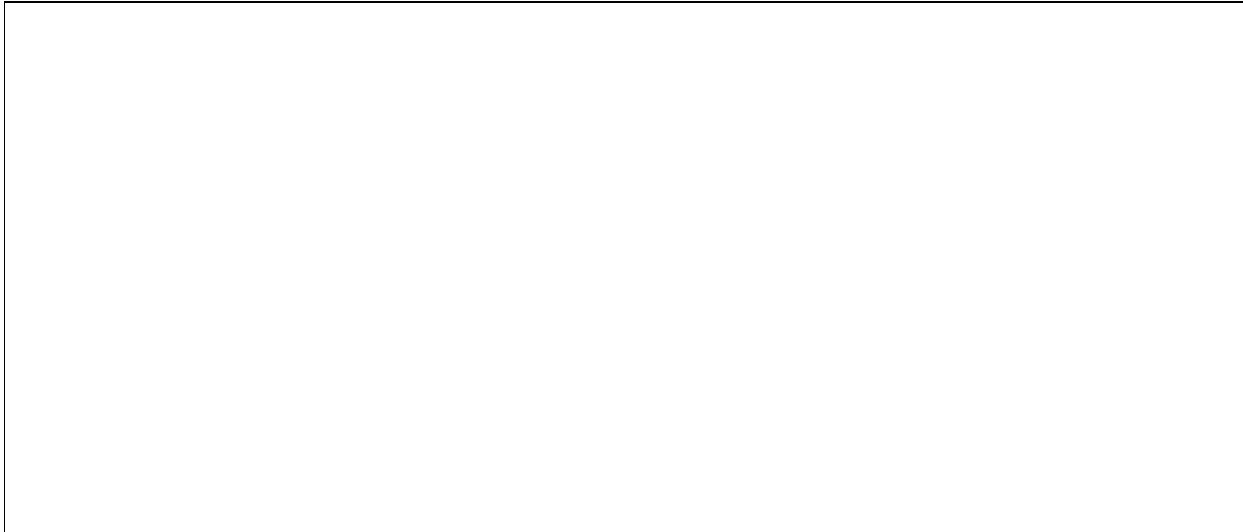
In the remainder of this section, attention will be given to the basic approach taken in Australia when responding to the four key elements identified above as being involved in determining intergovernmental transfer arrangements, and how this knowledge can inform the UK debate on a pathway to the reform of its current intergovernmental arrangements.

4.1 Grant management process

Too often, policy makers focus on outcomes rather than process. In the UK debate, while there is seeming agreement about the need for change in current grant allocation arrangements, there is a critical lack of accompanying discussion over the consultative framework for negotiating such transfers. This oversight is important as ‘process’ is everything when negotiating changes to intergovernmental agreements, especially on the sensitive issue of funding. Without due process, ownership and commitment from the parties involved will be missing. In the UK, grant levels are determined as part of the annual UK Government budget process and their level is not the subject of substantive consultation with DAs or England. Instead, the ‘top-down’ approach outlined in Figure 1 is applied with HM Treasury working with the UK Government to determine total expenditure by Department which directly impacts grant allocations to DAs and to England.

In the HM Treasury Statement of Funding Policy, HM Treasury sets out the arrangements which apply in setting devolved budgets. In addition, there is a Concordant between each DA and HM Treasury which sets out the relationship between HM Treasury and a DA Executive to ensure that both are aware of the requirements of the other and that both are consequently able to fulfil their responsibilities fully. This concordat is made in addition to any statutory arrangements for the provision of information to HM Treasury under the Acts which brought about the DA or as outlined in the Statement of Funding Policy. What results is at least twice-yearly, formal liaison meetings between HM Treasury and the DA Executive to ensure that there is co-operation between the two administrations and that the business of both operates effectively. This consultation is complemented by the Finance Director of the DA Executive being invited to attend HM Treasury’s regular meetings of Finance Directors of UK Government departments.

FIGURE 1: INTERGOVERNMENTAL CONSULTATIVE FRAMEWORK IN THE UK



Source:
HM Treasury (2007), *Funding the Scottish Parliament, National Assembly for Wales and Northern Ireland Assembly: Statement of Funding Policy*, October, (PU401) <http://webarchive.nationalarchives.gov.uk/+/http:/www.hm-treasury.gov.uk/d/pbr_csr07_funding591.pdf>
Concordat Between HM Treasury and the Scottish Executive (2005) <http://www.hm-treasury.gov.uk/d/scottish_executive_concordat.pdf p2> and <http://www.hm-treasury.gov.uk/psr_devolved_assemblies.htm>

This approach is a legacy of devolution in the UK which involves only a devolving of expenditure responsibility and a central role for HM Treasury. While it has the advantage of being administratively simple for HM Treasury and the UK Government, any push for greater devolution with the assignment of increased taxing powers and needs-based funding cannot be undertaken without a more open, transparent and consultative approach. Moreover, it will need to move from consultation between HM Treasury and the DAs to between the UK Government and the DA Executive.

In contrast to the UK, Australia has a long tradition of high level engagement between the Australian Government and State governments. This approach has its foundations in the Australian Constitution which made provision for transfers during the post-federation transitional period, following the loss by States of taxes to the Australian Government. In contrast, the unitary system of government in the UK has not required such a level of formal engagement with DAs.

Figure 2 outlines the consultative, advisory and performance assessment framework iur, train he a

FIGURE 2: INTERGOVERNMENTAL C

In Australia, while States in 2008-09 raised $50,118m or 14.8% of all tax revenue, their expenditure was $173,876m or 42% of all government expenditure. This was

With England having no representative assembly (a major focus of the 'West Lothian Question') unlike the DAs of Scotland, Wales and Northern Ireland, funding for public service delivery in England is determined by the UK Parliament and is assigned

In the recent past, this legitimate concern by Wales about being underfunded relative to Scotland when needs-based criteria are applied to grant allocation has been addressed through a Barnett Formula bypass. This was most evident when Wales secured Barnett Formula bypass from the UK government to enable the Welsh Assembly Government to access available European Union Structural Funds. Such an approach is a temporary solution to a known problem which can only worsen with the passage of time. Central to the problem for Wales is that the Barnett Formula is essentially an uplift regime for a needs-based grants distribution between the nations in the UK as determined in 1978. While the Barnett Formula can adjust for population changes between regions, it does not accommodate the changing needs of the different regions in the UK.

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FIGURE 5: HOLTHAM COMMISSION PROPOSAL TO REVISE THE BARNETT FORMULA

'Consequential' change (or additional spending made available) in the allocation to a Devolved Administration	=	Change expenditure on service in England*	X	Relevant 'comparability proportions' to England* by Devolved Administration	X	Relevant population proportion to England* by Devolved Administration	X	Needs adjustment term	X	Transition mechanism to account for any discrepancy between the needs-based assessment and the last block grant

* The base can in practice be England, England and Wales or Great Britain, depending on the coverage of the expenditure considered

Source: Holtham Commission(2010, p27)

It is this 1978 needs-based grant distribution that the Barnett Formula (Figure 4) is designed to update 'as if' the needs in 1978 applied today in each DA. Not surprisingly, with the passage of time, the Barnett Formula has proven increasingly controversial. In its Final Report, the Holtham Commission (2010)[33] strongly supported the introduction of needs-based funding of DAs and recommended the changes to the Barnett Formula shown in Figure 5. By introducing a 'needs adjustment term' which reflects per capita relativities in a DA relative to England (where this factor for England=100), changes in needs over time are introduced (but only at the margin). The Final Report of the Commission on Scottish Devolution (Calman Commission in June 2009)[34] and the Final Report of the House of Lords Select Committee on the Barnett Formula (July 2009)[35] also supported applying the principle of fiscal equalisation to grant distribution to DAs. In each Report, there was particularly strong support for the adoption of an approach similar to the independent advice provided by the Australian Commonwealth Grants Commission (CGC) to the Australian Treasurer on the allocation of general grants amongst States.

In the case of the Holtham Commission proposal in Figure 5, it would be the role of an independent statutory organisation (similar to the CGC) to advise the UK Government on the 'needs adjustment term'. Alternatively, if the Australian CGC approach was adopted, it would provide a 'needs adjustment term' for all regions of the UK, not just DAs. The response of the UK Government in December 2009[36] to the House of Lords Select Committee recommendation on the Barnett Formula (2009) was emphatic:

> 2.10 Recommendation: The role of the Commonwealth Grants Commission (CGC) in Australia offers a useful institutional model of an independent body that has responsibility for making recommendations about the allocation of finance. An independent body, similar to the CGC should be established in the UK. It should be the role of such a body to recommend the allocation of public monies based on population and through a needs based formula. Within the new framework the Treasury will need to retain its authority over the overall level of the block grant but not the proportionate allocation of the grant between the devolved administrations. This independent body might perhaps be called the

The Commission should be advisory in nature rather than have the power to make substantive allocation of funds on its own account. Its advice should, however, be published.

The remit of the Commission should be to determine the relative needs of each devolved administration on a regular basis, perhaps every five years. The Commission should also advise on the relative proportions of public spending for the devolved administrations, compared with spending within England, during a transitional period and recommend annual increments based on the latest population figures.

The Commission should be appointed by the UK Government as a non-departmental public body. It should be politically neutral and independent. It should be composed of a small number of members with sufficient expertise to ensure the dispassionate and authoritative nature of its work.

2.11 Response: The Government notes the Committee's views on the role of the Australian Grants Commission. Under the devolution settlements for Scotland, Wales and Northern Ireland the UK public expenditure framework and allocation me.8(I)5.5(r)-n4.8(I)5.5(r(tho) 1 I)g

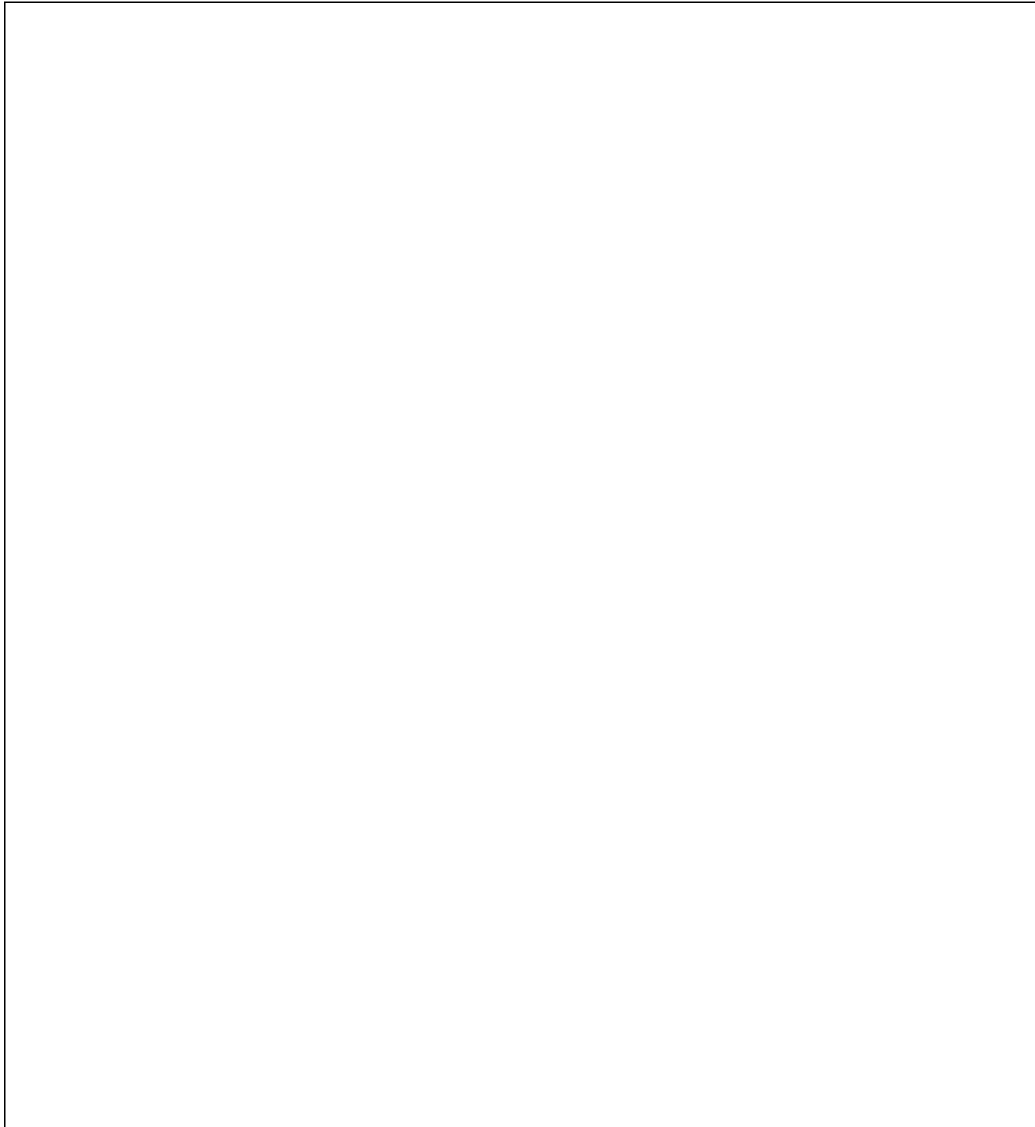
4. Potential costs of establishing and running such a system (including an independent advisory organisation (eg CGC) and the consultative framework (such as COAG).

These concerns are unreasonable and taken to their extreme, the basis for never changing current arrangements, no matter how unjustifiable in theory and practice. In relation to (1), this is true of most change but the solution lies in how the process is managed. On (2), this is contradicted by the seemingly uncontroversial and politically accepted operation of an already complex fiscal equalisation arrangement for the allocation of grants to local government. In the case of England's local government,

the basis for the UK Government's continued support for the Barnett Formula despite the general chorus call for change. In particular, that:

1. Barnett Formula is simple and with Barnett Plus, flexible, whereas a needs-based arrangement would be complex and far less simple;
2. Barnett Formula places greater control of both the quantum and distribution with the central government (and HM Treasury);
3. Central government concern that sub-central governments might not be accountable given they do not have substantial revenue ('hard budget constraint' issue) or expend untied general grants according to national principles ('National Priorities').
4. That while ever England is not a DA, the allocation to the current three DAs could not take place without effectively modelling England as if it was a DA. This has the potential to duplicate (and possibly conflict with) the needs-based approach to allocating grants to English LG.
5. That despite the House of Lords Final Report asserting that the new system should not duplicate what DAs currently do for LG when determining their grant entitlement, this is a real possibility when the LG has essentially an agency relationship with the DA[42]. In effect, moving to needs based grant allocation at the DA level and the DA's grant allocation framework for LG funding would need to be consistent. Since DAs 'pass-through' a substantial proportion of their DA funding from the UK Government to LG, anything else would lead to inconsistencies.
6. Identification of needs is of0 Te23 69avoi7(')de gJ17.1420le roj/TT4 particu3 Tw[y)-7.6(m)3(li

FIGURE 7: GENERAL GRANT ASSESSMENT FRAMEWORK IN AUSTRALIA



The 'Total Requirement for Financial Assistance' is therefore a measure of the total funding required by States who make an 'average' effort to raise own-source revenue and have acknowledged any disabilities impacting service delivery and infrastructure provision. In offsetting against this funding 'Requirement' the 'Revenue assistance from Australian Government Payments' (or NSPP, NPP and NHHNF), the CGC methodology effectively undoes the distribution amongst States of any special negotiations between the Commonwealth and the States in terms of the allocation of specific grants. However, the Commonwealth Treasurer in his TOR to the CGC has

element in bringing about positive reforms and from which the UK can learn much in terms of how to manage the process of change during a period of budgetary crisis.

If the UK Government moves to reduce funding to DAs or force tax reassignment without addressing inequities in the distribution of current grants, it can only expect division and dissent and a risk to the stability of the union. The new UK Government's stated commitment to a commission in Wales along similar lines to the Calman Commission in Scotland will undoubtedly reach similar conclusions to the

Since no system can be designed without the need for constant refinement, (S4) highlights the importance of constant review. In the case of (S1), a flexible arrangement permits its constant review and updating. In relation to (S2), the Holtham Commission (2010) proposed that the revised Barnett Formula (Figure 5) be reviewed each decade. Australia reviews its CGC arrangements every 5 to 10 years. In the case of tax and expenditure reform, Australia has routinely reviewed key aspects of its tax system every 7-10 years.

Over the coming decade, the nations in the UK union will confront a continuing budgetary crisis. In such an environment, any deficiencies in current arrangements will become potentially the source of failure and division within the union. The danger for the UK Government is that as it moves to greater devolution accompanied by tax reassignment and expenditure devolution (S3) during a period of budgetary crisis, that the weaknesses in the current intergovernmental arrangements (S2) will become exacerbated. Open and transparent government based on an informed and consultative decision making approach (S1) will do much to reduce policy-on-the-run and lack of broad support so often a characteristic of crisis policy making.

What the discussion in this paper has highlighted is that any move to further devolution and tax assignment in the UK, especially in an environment characterised by substantial budget deficits, will invariably force necessary institutional change. However, institutional change is typically slow to occur especially where change brings with it reduced influence by key participants (such as the UK Government and especially HM Treasury). What is different though about 2010 is that the UK government has committed to addressing its budgetary crisis and furthering devolution while the devolved governments are demanding a restoration of needs-based grant funding and the assignment of taxing powers. Resolving these potentially conflicting demands would be greatly facilitated through an open and consultative process on engagement by nations in the UK union. Here, the UK has much to benefit from building on the approach taken in the Australian federation (S1, S2, S3 and S4) to managing competing interests and demands across federation members during periods of major change. Change without attention to process and pathway risks divisiveness (and failure) at worst and delayed implementation at best. The UK does not have the luxury of time and the current crisis is the perfect environment in which to implement reforms which require major institutional change.

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