



STRATEGIC REVIEW OF
**The Administration of Australian Government
Grant Programs**

31 JULY 2008

MR PETER GRANT PSM



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Department of Finance and Deregulation
Financial Management Group

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EXECUTIVE SUMMARY

Introduction

A comprehensive review of the administration of Australian government grant programs

The Government has commissioned a comprehensive strategic review of the administration of Australian Government grant programs, to be managed by the Department of Finance and Deregulation (Finance). The objective is to improve efficiency, effectiveness, accountability and transparency in the administration of grant programs across the Commonwealth. This report addresses the first element of the review, and makes a series of recommendations for improvements to the current policy framework for the administration of grants.

Commonwealth grant programs: scale and characteristics

Grant programs take many forms, and serve many different purposes

Grant programs vary widely in their form, scale and degree of complexity. Some provide short-term, one-off support or assistance to grant recipients, with only a broad specification of purposes and quite simple accountability requirements. Other programs are project-based, of longer duration and with a much tighter specification of deliverables. Other programs again support the ongoing delivery of services, with funding provided to the same or similar organisations more or less continuously over a period of years. It is very difficult to generalise in the grants domain: for every general observation made, there will inevitably be some significant exceptions.

Data sources are patchy...

There is no single, comprehensive source of data on the number of individual grant programs, the number of grants awarded or the total scale of grant program funding across the Commonwealth. Data need to be compiled from a number of different sources, and even then, a significant element of estimation is necessary.

...but the scale of grant funding is substantial...

More than 49,000 'discretionary grants' were approved in calendar year 2007 under some 250 separate funding programs, to a total value of more than \$4.5 billion. In addition, more than 90 Commonwealth specific purpose payments (SPPs) were made to State, Territory and local governments, involving total expenditure some \$32 billion. Taking both these funding sources in combination, and allowing for other grant programs not included within the scope of these aggregates, current Commonwealth expenditure on all forms of conditional grants is likely to be between \$40 billion and \$50 billion annually, or about one-sixth of total Commonwealth outlays.

...with more than \$40 billion spent on all forms of conditional grant each year

Spending on 'discretionary grants' in particular has grown strongly...

Both the number and value of discretionary grants awarded have grown strongly in recent years – from fewer than 4,000 grants with a total value of about \$580 million in calendar year 2000 to around 49,000 grants with a total value of \$4.5 billion in calendar 2007. Moreover, growth accelerated in the latter part of this period: between 2006 and 2007, for example, the number of discretionary grants more than doubled, and the total value of funding approved grew by more than 60 per cent, on a like-to-like basis.

...especially in more recent years

Policy context

The ANAO's audits of grant programs have raised major issues...

...going both to the administration of individual programs and the adequacy of the current policy framework

Audit criticisms have been strong and numerous

A new emphasis on higher standards of transparency and accountability, and evidence-based policy

The focus here is on discretionary grants rather than SPPs ...

...although similar principles apply in both cases

The administration of Commonwealth grant programs has been the subject of significant audit activity, and related parliamentary scrutiny, in recent years. The Australian National Audit Office (ANAO) has conducted more than twenty performance audits of grant programs since 2004–05. Many of these audits have raised significant issues going both to the overall framework for the administration of grant programs and to the quality of administration of individual programs. In some cases, the ANAO has gone so far as to conclude that an agency's administration of a grant program has fallen short of an acceptable standard of public administration.

Major issues and criticisms raised in the ANAO's reports have included deficiencies in the application of the financial framework governing the expenditure of public money; weaknesses in program planning, design and decision-making processes; deficiencies in program guidelines; flaws in procedures for selecting grant recipients and projects, and a more general lack of transparency; a lack of effective documentation, especially of the reasons for key decisions; weaknesses in funding agreements, including a lack of clarity as to the roles and responsibilities of different parties; a lack of effective oversight of funded projects; and major weaknesses in performance monitoring, evaluation and accountability arrangements.

The new Government has made strong commitments to improve standards of transparency and accountability in public administration generally, and to ensure that policy making is soundly evidence-based. The review team has been mindful of these commitments in undertaking its work and developing its recommendations.

Scope and focus of the review

The Review has focussed principally on those grant programs commonly described as 'discretionary'. Most of the issues raised in the ANAO's audit reports have arisen in this sphere, rather than in the domain of SPPs; moreover, SPPs are currently subject to a separate process of review and reform as part of the new framework for federal financial relations agreed by the Council of Australian Governments.

Unless otherwise stated, the recommendations made in this report relate to discretionary grant programs which are conditional in nature but are outside the scope of the current SPP reform process. That said, most of the key principles underlying the report's recommendations apply equally to many SPP grant programs, subject only to any specific provisions contained in a program's governing legislation.

Framework requirements for effective grants administration

Four key framework requirements

The Review has identified four key ‘framework’ requirements which need to be in place in order to support the effective administration of grants across the Commonwealth. These are:

- > a standard framework of concepts, definitions and classification principles, providing a common understanding of the meaning of terms and a clear basis for the interpretation and application of policy guidance;
- > a clear framework of policy principles governing the administration of grant programs across the Commonwealth;
- > a strong financial management framework, with clear links drawn between the requirements of that framework and the responsibilities of decision-makers and others involved in the administration of grant programs; and
- > a robust framework for the collection and reporting of statistical and other information on Commonwealth grants, designed to meet both administrative requirements and public accountability objectives.

There are important gaps and weaknesses in each of these respects.

Concepts, definitions and classification principles

There is no common language on grants...

A major gap in the current framework is the lack of any common language of communication on grants across the Commonwealth. No standard set of definitions or classification principles is in place, and there is no common understanding as to what exactly constitutes a ‘grant’ or a ‘grant program’. There is little clarity, let alone consensus, as to what key features should distinguish a ‘grant’ from a ‘gift’, ‘procurement’ or other form of financial transaction. Widespread inconsistency and potential for confusion is the result.

...nor any agreement on key definitions and classification principles

Practices vary widely across agencies...

In the absence of any whole-of-government guidance on these matters, individual agencies have developed their own classification practices and, to some extent, their particular classification cultures. On the border between grants and procurement, for example, some agencies choose to err on the side of procurements rather than grants, whereas others opt the other way. Convenience rather than principle has often been at work: for example, some agencies have openly acknowledged that a factor underlying their large number of grant programs has been a wish to avoid the application of the *Commonwealth Procurement Guidelines*. There is no effective mechanism of central oversight or scrutiny of agencies’ decisions in these respects.

...and there is no central oversight of agencies’ decisions

Whole-of-government guidance is needed for reasons of clarity and consistency ...

The Review’s major conclusion in this area is that Finance should issue overarching, whole-of-government guidance covering the definitions of each major class of Commonwealth financial transaction, including grants, and the principles to be applied in determining the appropriate classification of any individual transaction. The objective should be to provide better guidance to agencies in reaching their classification decisions; promote greater consistency in classification procedures across the Commonwealth as a whole; and ensure that the appropriate policy framework is applied to any given transaction, consistent with its essential characteristics.

... and to ensure that the appropriate policy framework is applied

A policy framework for grants administration

There is no Commonwealth-wide policy framework for the administration of grants

There is no whole-of-government policy framework in place for the administration of grants across the Commonwealth. Individual agencies have issued policy guidelines, but these are agency-specific, vary widely in their terms from agency to agency, and do not represent a whole-of-government policy framework in any sense. The lack of any Commonwealth-wide policy guidance on grants is a major gap in the overall framework for grants administration, especially in view of the significant problems which have arisen over recent years.

The ANAO's Better Practice Guide is an important source of practical guidance...

The ANAO's *Better Practice Guide* has come to be used, virtually by default, as the *de facto* statement of Commonwealth policy requirements in relation to grants. Valuable as the *Better Practice Guide* has been, it is not designed as a policy document as such: rather as a means of assisting agencies to improve their administrative performance and management practices. Any central framework of policy guidance on the administration of grants should properly be determined and promulgated by the Government itself.

...but policy should be set by the Government itself

The policy framework governing Commonwealth procurement activity is sound...

The analogy with procurement is relevant here. A whole-of-government policy framework is in place for procurement, in the form of the *Commonwealth Procurement Guidelines* (CPGs). The CPGs have legislative authority, being issued by the Finance Minister under the FMA Regulations, and officials performing duties in relation to procurement are required to have regard to the CPGs.

...and similar arrangements should be put in place for grants

Similar arrangements should now be put in place in relation to grants. A key first step would be to develop and implement a whole-of-government framework of policy guidance on the administration of grant programs. As in the procurement setting, the framework should be largely principles-based, with prescriptive rules and mandatory requirements kept to a minimum. Like the CPGs, the new grants policy framework would have legislative authority, and officers responsible for the administration of grants would need to have regard to the terms of that framework in carrying out their duties.

The Better Practice Guide should then serve as an important companion document to the policy framework

There would still be a valuable role to be played by a publication such as the ANAO's *Better Practice Guide*, but as a companion document to the whole-of-government policy framework rather than as a free-standing document in its own right.

Financial management framework

The Commonwealth's financial management framework is strong...

The *Financial Management and Accountability Act 1997* (FMA Act) provides the central legal framework for financial management within the Commonwealth. This legislation, along with its supporting FMA Regulations and FMA Orders, sets down the fundamental principles and essential rules to be followed in managing the Commonwealth's resources. The FMA legislative framework applies to all proposals and decisions to spend public money, including grants, and makes no specific reference to grants as such.

...but there has been confusion and uncertainty about its application in the grants domain

A recent Finance Circular provides helpful guidance...

...addressing a number of the issues raised in ANAO audit reports

The structure of the FMA Regulations adds unnecessary complexity...

...and should be reviewed

There are major weaknesses in the information collected and reported on Commonwealth grants

A unit should be established within Finance to coordinate the development of a whole-of-government policy framework for grants...

...and to work closely in consultation with line agencies

Despite the strength of the Commonwealth's financial management framework generally, there has been some significant uncertainty about aspects of its application in relation to the administration of grant programs. Key areas of uncertainty and confusion have been highlighted in a series of ANAO audit reports.

Finance has recently issued an important Finance Circular designed to assist FMA Act agencies to understand and comply with their obligations when making commitments to spend public money. Although not focused specifically on the area of grants, this Circular usefully covers a range of issues which have been raised in the ANAO's audits of grant programs in recent years: for example, it includes advice on the role to be played by agencies when advising their Ministers on the exercise of their responsibilities as approvers of spending proposals. This latest guidance should assist agencies in understanding the requirements of the financial management framework and in applying those requirements in their particular program setting.

One factor which adds unnecessary confusion and complexity in these matters is the structure of the FMA Regulations themselves. Part 4 of the Regulations, relating to commitments to spend public money, is unduly complex in its current form, and the sequence of individual Regulations does not align well with the order in which key administrative processes typically occur, or need to occur. There is scope to shorten and simplify the current set of Regulations in this area with a view to improving their logical sequence, increasing their clarity, and promoting consistency of interpretation and application by agencies. This process should be completed by June 2009.

Information collection and reporting

Another major gap in the current framework for grants administration relates to arrangements for the collection and reporting of information on grants across the Commonwealth. Current arrangements for information collection and reporting on grants meet neither the Government's own information needs nor the wider objectives of transparency and public accountability. These matters are discussed in more detail below (see *Disclosure and reporting arrangements*).

Investing in a new grants framework

A significant investment of resources will be needed to address these serious deficiencies in the current framework for the administration of grants. A dedicated unit should be established within Finance to coordinate the development of a new policy framework for grants administration and to oversee its implementation across the Commonwealth. The new unit should consult closely with line departments and agencies during the development phase of its work and, once a new policy framework for grants has been endorsed by government, it should actively engage with agencies both to explain the terms of the new framework and to assist them in implementing its requirements.

This investment will entail some short-term costs...but there will be net benefits in the longer term

There will be a cost attached to this investment of resources, especially in the developmental phase, but this should be significantly outweighed by the long-term benefits which will accrue from a robust whole-of-government framework for the administration of grants.

Planning and decision-making arrangements

Planning and assurance issues

Effective planning is critical to the success of a grant program...

High-quality planning is critical to the success of any grant program. The key objective of the planning process should be to ensure the program is appropriately structured to achieve its intended outcomes, and will be managed in an efficient and effective manner. Transparency in decision-making and accountability for the use of grant funding should be paramount considerations.

...but planning processes have often been seriously flawed

The ANAO's recent audit reports provide numerous examples of grant programs in which agencies' planning processes have been seriously flawed, often in multiple respects; specific examples are cited in Chapter 3 of the report. In many of these cases, the major problems encountered at a later stage in program administration could have been averted, or significantly ameliorated, had planning processes been more systematic and thorough at the outset. Much stronger assurance is needed that all key considerations relevant to the planning of an efficient and effective grant program have been fully and systematically addressed.

Much stronger assurance is needed before programs are implemented and money is spent

The need for better planning and stronger assurance was highlighted in the Government's decisions taken in December 2007, designed to strengthen the management of discretionary grant programs across the Commonwealth. One of those decisions introduced a requirement that guidelines for any new discretionary grant programs must be considered by the Expenditure Review Committee of Cabinet (ERC).

The information requirements accompanying new policy proposals should be strengthened...

The Review supports strongly the intended purpose of this requirement, but questions whether it is the most efficient means of providing ERC with the assurance that it needs. As an alternative, it suggests that the information to be reported as part a new policy proposal should be designed to provide assurance that a robust planning process has been undertaken, and that the proposed grant program is appropriately structured to achieve its intended outcomes.

...and funding approvals given only when there is confidence that a robust planning process has been completed

Where the information supporting a new policy proposal is not adequate to provide the level of assurance required, any approval of a new grant program should be made on an in-principle and conditional basis only, on the understanding that no payments would be made under the program until the responsible Minister had provided evidence that a robust planning process had been completed. Where additional assurance was needed in any particular case, it would be open to ERC to require the submission of draft program guidelines (or other appropriate evidence) before the program was formally implemented and any payments made.

Decision-making in grant programs has been a matter of strong public interest and significant scrutiny...

...and legitimately so

The Government has acted to strengthen the quality of decision-making in grant programs

Decision-making in grant programs

Decision-making in grant programs has been a matter of strong public interest, widespread parliamentary and audit scrutiny, and significant political contention in recent times. The reasons for this lie largely in the 'discretionary' nature of many grant programs, the high levels of flexibility built into application assessment procedures, and the consequent lack of transparency in many decision-making processes. Perceptions that extraneous factors have played a part in grant decision-making processes have been heightened by the findings of some recent ANAO performance audits, which have established a strong statistical relationship between the relevant Ministers' influence on funding decisions and the electorates to which grant funding has been directed.

With a view to strengthening the quality of decision-making in grant programs, and improving public confidence in the process, the Finance Minister's Instructions issued in December 2007 introduced a number of new controls on Ministerial approval of discretionary grants. There were three main elements to the new decision-making rules, as follows:

- > Ministers are not to make decisions on discretionary grants without first receiving departmental advice on the merits of the grant application.
- > If a Minister chooses not to follow departmental advice, the decision to award or reject a grant should be referred for determination by a Ministerial Group, following a written submission from the relevant Minister providing reasons as to why a decision should be made against departmental advice.
- > Ministers who are members of the House of Representatives are not to make decisions in relation to grants in their own electorate, even on the basis of departmental advice; instead, these decisions also are to be taken by the Ministerial Group.

The Minister for Finance and Deregulation (Finance Minister) has noted publicly that these should be considered interim arrangements, pending the outcomes of the current review. Accordingly, the Review has considered the merits of the new decision-making rules, including their likely practical implications and consequences.

Consideration of departmental advice

Ministers should continue to receive departmental advice before taking their decisions on grant applications...

...including in cases involving election commitments

The Review supports retention of the first requirement above: namely, that Ministers should not make decisions on discretionary grants without first receiving departmental advice on the merits of the grant application. This is a prudent control, designed to ensure that where Ministers elect to assume a decision-making role in relation to the award of grants, they are well-informed of the department's assessment of the merits of grant applications and suitably briefed on any other relevant considerations. The requirement for prior consideration of departmental advice should apply to all grant spending proposals, including those made in the context of an election campaign.

Decisions taken at variance with departmental advice

It should be open to a Minister to reach a different decision from that recommended in departmental advice...

...but special care will be needed in these cases

Where Ministers take a different view, they should clearly over-rule their department and document the basis on which they have reached their decision

Different conclusions can be drawn, quite legitimately, from any given set of information and evidence, and it should be open to a Minister to reach a decision different from that recommended in a department's or agency's advice. In view of the sensitivity likely to attach to such decisions, however, special care will be needed in these cases in order to demonstrate that the relevant program guidelines and selection criteria have been observed, that all grant applicants have been treated fairly, and that the requirements of the financial framework have been met.

In these circumstances, where a Minister disagrees with an agency's assessment and recommendation on a particular grant application, the Review considers that it would be appropriate for the Minister to clearly over-rule the department and document the basis on which the Minister has reached an alternative view. It should no longer be acceptable, as has happened in the past, for a Minister to decline to document reasons in such circumstances; for a Minister to ask the department to restructure its advice and recommendations to accord with the Minister's views and preferred outcomes; or for a department to 'retro-fit' its documentation or records merely to comply with a Minister's wishes or proposed changes, rather than to execute a Ministerial decision.

Responsibilities for decision-making on grants

The referral of sensitive decisions to a Ministerial Group is likely to create some unintended and undesirable consequences

The risks associated with these decisions will best be managed by those Ministers with formal responsibility and detailed knowledge of the program in question

The Review is not persuaded that the referral of sensitive and potentially controversial decisions to a committee of Ministers (Ministerial Group) would lead to an improvement in the quality or efficiency of decision-making on grants. On the contrary, its analysis suggests that this arrangement would be likely to create a range of unintended and undesirable consequences, including some significant inefficiencies.

In the Review's judgement, the risks associated with such decisions – for example, those in which a Minister forms a view at variance with departmental advice – will best and most appropriately be managed by those Ministers with formal responsibility and detailed knowledge of the grant programs in question. In support of this view, it considers that there are other, more efficient ways to strengthen the quality of decision-making in grant programs, and to improve the level of public confidence in those decisions. A requirement to document the reasons for decisions, as discussed below, is one such measure.

Similar considerations apply in the case of decisions involving grants within a Minister's electorate. While accepting that these decisions are likely to be sensitive and subject to considerable scrutiny, the Review does not see a strong case to remove such decisions from the power of the responsible Minister, especially in view of the large number of such cases which could be expected to arise in the normal course of business in any year.

Documentation of decisions

It is critical that agencies have a clear understanding and record of Ministers' decisions on grants...

Given the fundamental importance of the approval process in relation to the expenditure of public funds, and for accountability purposes, it is critical that agencies have a clear understanding and record of Ministerial decisions. In that context, the recording of the reasons for Ministers' decisions to approve or not approve a grant application has been widely recognised as sound administrative practice, including in the views expressed by a number of Parliamentary Committees.

...but there is no requirement under current policy for decision-makers to document the reasons for their decisions

Under current policy, however, there is no requirement on Ministers (or other approvers) to document the reasons for their decisions, as distinct from the terms of those decisions, even in cases where they take a different position from the advice presented to them. While it is open to an agency to invite a Minister to document his or her reasons for a funding decision, and this has sometimes been done, it is equally open to a Minister to decline such a request, and this also has been done.

There is a strong case to introduce a new requirement on the approvers of grant program spending to document the basis, as well as the terms, of their approvals

In view of the clear evidence of irregularities in past decision-making on discretionary grants, and given public concerns in this respect, the Review considers that there is a strong case to mandate a new requirement on the approvers of grant program spending under FMA Regulation 9 to document the *basis*, as well as the *terms*, of their approvals. In most cases this could be achieved quite simply and effectively by the insertion of a standard clause in the terms of the briefing advice presented to the decision-maker. Where a decision is taken at variance with the briefing advice and recommendation, however, or where the reasons for a decision differ from those cited in the briefing advice, a documented explanation of the reasons supporting the final decision would be required.

This requirement should be quarantined to the grants domain

In order to quarantine this new requirement to the grants domain, the Review proposes that it be implemented by means of a specific provision inserted into the terms of the FMA Regulations authorising the new whole-of-government grants policy framework.

Approval of multi-year discretionary grant programs

The requirement to seek prior approval for certain multi-year discretionary grants...

Under current policy, the prior approval of the Finance Minister is required for any multi-year discretionary grant exceeding 36 months in duration and/or \$2 million in value, unless a specific exemption has been granted in advance. The nominal purpose of this requirement is to regulate the extent to which agencies can commit future year budget funding.

...serves no useful purpose...

The Review has examined the rationale for this requirement and concluded that it serves no useful purpose. There is no known instance in which an application for approval has been declined under these arrangements; moreover, the approval process effectively duplicates another process of approval by the Finance Minister, under FMA Regulation 10, and thereby creates both a significant administrative burden and unnecessary red tape.

...and should be abolished

The Review recommends that the approval process for multi-year discretionary grants should be abolished.

Provision of grant funding outside regular program guidelines

There are particular risks involved in cases where Ministers wish to award a grant outside regular program guidelines...

The situation has sometimes arisen, especially in grant programs involving a high degree of discretion, that a Minister wishes to award a grant to a particular organisation or recipient outside of the regular program guidelines. Proposals of this nature may put the integrity of the selection process at risk, and raise significant issues of transparency and accountability. They can also place pressure on the relationship between a Minister and an agency.

...this should only occur where there is explicit authority to do so...

The Review considers that, should a Minister wish to have the flexibility to provide grant funding outside of regular program guidelines and processes, this intention should be made transparent in the design of a grant program and authorised specifically in the terms of Cabinet's approval. Any limits on a Minister's powers to exercise this flexibility (for example, limits on the maximum size of any individual grant, or on all such grants in aggregate) should also be specified in the terms of the Cabinet's approval. An arrangement broadly along these lines already operates within the overseas aid budget, in the form of a 'Mandated Flexibility' allocation.

...and within any specified limits...

...and subject to the usual requirements

As in the case of any other grant spending proposal, a Minister responsible for approving a spending proposal under these arrangements would be required to ensure that the proposed expenditure represents an efficient and effective use of public money and is in accordance with the policies of the Commonwealth. A documented statement of reasons would also be required.

Disclosure and reporting arrangements

Effective disclosure and reporting on grants is essential...

Effective disclosure and reporting arrangements are essential both for the Government's own purposes and for reasons of transparency and public accountability. A comprehensive, whole-of-government reporting framework is a key requirement if government is to be well informed in the decisions it makes both on individual grants and on grants policy generally. Over and above this need, easily accessible information on the availability of grants and the details of grants awarded is a precondition for public and parliamentary confidence in the quality and integrity of grants program administration. On neither count are current arrangements satisfactory.

...both for the Government's own purposes...and for transparency and public accountability reasons

...but current arrangements are quite unsatisfactory, and serve neither purpose well

While there are many different sources of information on Commonwealth grants, there is little coherence in the overall structure of that information, particularly from a public accountability viewpoint: even if it were possible to know of and gain access to all the sources of published information, it would be impossible to compile a comprehensive and reliable picture of grant program activity across the Commonwealth.

Discretionary Grants Central Register

The Discretionary Grants Central Register is a poorly-designed system...

...with many limitations...

...which fails to meet even its own stated objectives

It also fails the transparency test, making no provision for public access to the information collected

A new reporting system is needed ...

...comprehensive in its coverage...

...and designed to meet the full range of whole-of-government reporting requirements on grants

Strong quality controls will be needed...

...as well as assurance that the new system is both well-designed and robust

Finance manages a central database called the Discretionary Grants Central Register (DGCR), but this system suffers from a range of serious limitations. It is a highly cumbersome system, with poor functionality and limited analytical capabilities. It is poorly connected with line agencies' own information systems, and places a heavy administrative burden on reporting agencies. The coverage of the register is not comprehensive, and the data captured are of highly variable quality.

The Register fails to meet even its own stated objectives. A key design objective was to control the incidence of 'double-dipping' of grants by organisations applying for grant funding under different programs or across different agencies for the same or closely related purposes. Finance has advised, however, that there is no known case over the past 10 years in which such 'double-dipping' behaviour has been averted by the use of information on the DGCR.

Another major limitation of the DGCR is that its use is confined to government alone, with no provision made for public access to the information collected. This contrasts with the AusTender reporting system operating in the procurement area, which was specifically designed to meet transparency and public accountability objectives.

A new reporting system on grants

For these reasons, and others, a new reporting system should be developed to meet both whole-of-government requirements for information on grants and a range of public information, transparency and accountability objectives. The new system should be developed in close consultation with agencies, and be comprehensive in its coverage of all grant programs and grants awarded. It should provide online public access to information on Commonwealth grant programs, forthcoming grant selection processes, and details of grants awarded; for this purpose, agencies should be required to lodge details of any grant awarded within two weeks of the signing of a funding agreement.

The new reporting system should be designed to meet the full range of whole-of-government reporting requirements relating to grants (such as Annual Report requirements and Senate Order 192 requirements). The system should also have regard to experience gained with the operation of AusTender system for procurement reporting, and be compatible with the design of that system as far as practicable.

It will be important to be able to demonstrate that the new reporting system is both well-designed and robust. Strong data quality standards and data entry protocols should be developed, supported by effective quality assurance procedures. In addition, the Australian National Audit Office should be invited to conduct a two-stage audit of the new system: the first at the detailed design stage, before full implementation, to provide assurance that the system is structured appropriately, in line with its intended objectives; and the second at the post-implementation stage, to provide assurance that the new system is operating efficiently and effectively.

Once these requirements have been satisfied, existing reporting systems should be dismantled...

...and current reporting requirements reviewed

Once there is adequate assurance in these respects, the Discretionary Grants Central Register should be decommissioned and dismantled, along with the GrantsLINK system managed by Infrastructure (to the extent that it serves as a whole-of-government reporting system).

There will be a powerful case also to review and rationalise the array of whole-of-government reporting requirements in relation to grants, having regard to the high-quality information which should be made available under the new reporting system. Current reporting requirements are uncoordinated and piecemeal, meeting none of their intended purposes either comprehensively or particularly well; in the case of annual reports, for example, there is little by way of meaningful information, reported on a consistent basis, across the Commonwealth. At the same time, the Senate should be invited to review the operation of, and continuing need for, Senate Order 192.

Funding agreements for grants

Effective funding agreements are essential...

A funding agreement is a document signed by the funding provider and a grant recipient setting out the terms, conditions and arrangements under which a grant is to be provided, received, managed and acquitted. Funding agreements may take a variety of forms – a letter of offer, a contract, a deed of agreement, or a memorandum of understanding (MOU) – depending on their substance and characteristics.

...to promote the efficient, effective and ethical use of Commonwealth resources...

Effective funding agreements are critical to promote the efficient, effective and ethical use of Commonwealth resources. A funding agreement for a grant program should contain appropriate controls and accountability mechanisms to ensure that grant funds are spent appropriately and that deliverables will be provided within budget and on time. Funding agreements help to manage risk and resources, specify responsibilities, and set reporting, acquittal and record-keeping requirements. A well-designed funding agreement will also establish the basis for a constructive and cooperative relationship between the grantor and the recipient, providing clarity of objectives and a shared set of understandings and expectations.

...and to manage the relationship with a grant recipient

Common-sense principles apply...

Some common-sense principles apply to the design of funding agreements. For example, no payments should be made to a grant recipient until the funding agreement has been signed, and subsequent payments should be structured according to need. Start-up payments should be limited to cases in which they are specifically required, and deliver a net benefit to the Commonwealth. In the case of large-scale projects involving high-value grants, funding should be paid progressively as milestones are reached and deliverables received; final payments should be tied to the submission of final product, to an acceptable level of quality.

...to the design of payment arrangements...

...the setting of conditions...

Similarly, the funding agreement is critical in establishing the rights and obligations of the Commonwealth, the conditions to be met by the grant recipient, the terms on which its provisions are enforceable, and the remedies

...and the stipulation of remedies for breach or default...

available in the event of any non-compliance. Grant monies must be recoverable, or other remedy available, in the event that a grant recipient is in breach of the conditions of grant. All funding agreements should be drafted to ensure enforceability at law.

...but problems continue to emerge in some grant programs

Problems arise where these common-sense conventions are not observed, as highlighted by several recent ANAO performance audits. A failure to put in place an effective funding agreement, or to manage that agreement once it is in place, can put a project at risk of not meeting its objectives, and the Commonwealth at risk of not using its resources in an efficient, effective and ethical manner.

As grant programs vary widely...

Grant programs vary widely in their scale and degree of complexity, from simple grants for small amounts to community or voluntary organisations to large-scale funding for complex projects – for example, major infrastructure projects with elaborate governance structures, multiple funding partners and high levels of risk.

...‘proportionality’ principles should be applied...

No one form of funding agreement will be appropriate in all circumstances: rather, the principle of ‘proportionality’ should be applied, so that funding agreements are tailored to reflect considerations such as the purpose, value and duration of a grant, the deliverables to be supplied, associated conditions of grant, the level of enforceability required, and the nature and level of the risks involved. In the case of grants involving complex commercial transactions, for example, funding agreements should be individually structured to reflect the role, responsibilities and level of control which each of the parties to the agreement is expected to assume.

...so that funding agreements are tailored to suit the characteristics of the grant and the level of risk involved

Plain English should be used, and complexity avoided, as far as possible

Funding agreements have become increasingly long and complex documents – in some cases, quite unnecessarily so. Without compromising the principles of enforceability and proportionality, funding agreements should be cast in plain English as far as possible, with a minimum of complexity and legal jargon.

The form of funding agreement to be used should be chosen to reflect the nature of the grant in question

Proportionality principles should also guide the choice of the particular form of funding agreement to be used:

- > funding agreements for small-scale, one-off grants should generally take the form of a simple **letter of offer** (having regard, in the drafting of any such letter, to the elements of contract formation and considerations of enforceability);
- > **contracts** should be used in the case of large-scale or complex grants, such as grants for the funding of major infrastructure projects involving high levels of conditionality and multiple funding partners;
- > **deeds** should be recognised and promoted as a legitimate form of funding agreement, especially in the case of medium-sized grants or in circumstances in which there may be room for doubt as to the enforceability of a contract (for example, due to a lack of consideration or a lack of intention to create legal relations).

Finance should provide guidance to agencies on these matters

To assist agencies in these matters, Finance should produce a checklist of issues to be considered in the development of a funding agreement for a grant. It should also arrange for guidance to be issued on the use of deeds as funding agreements, and the circumstances in which the use of deeds may be appropriate.

Performance measurement and assessment

Performance measurement and assessment have been an ongoing issue in grant programs...

Performance measurement and assessment have been a major, ongoing issue in the administration of Commonwealth grant programs. Successive ANAO audit reports have highlighted multiple weaknesses in this regard, such as failures to collect basic data; to identify objectives that are distinct and measurable; to develop meaningful and adequate outcome indicators (including, in some cases, any measures of effectiveness); to establish a baseline against which progress can be monitored; and to report on program performance in Annual Reports. These weaknesses are not matters of dispute or contention: for example, all of the audited agencies have acknowledged the validity of the ANAO's criticisms and agreed with its recommended actions in response.

...with serious weaknesses evident across a wide range of programs and agencies

Effectiveness of grant program spending

Weak performance measurement means that judgements on program effectiveness often cannot be made...

An important consequence of these major weaknesses in performance measurement is that, in many cases, there is no reliable basis on which to assess the impact, efficiency or effectiveness of a grant program: the data required to make such judgments are simply not available.

...but circumstantial evidence suggests that the quality of grant program spending has often been poor

The Review has not attempted any detailed assessment of the effectiveness of individual grant programs. To the limited extent that any judgements can be made on these matters, however, there is strong circumstantial evidence to suggest that much grant program spending in recent years has been of poor quality, and probably ineffective in many cases. Such evidence includes, for example, the rapid increase in the number of grant programs overall, and in the number of individual grants awarded; major weaknesses in program planning and design; a lack of clear objectives for some programs; the frequent absence of detailed performance information, effective monitoring arrangements or proper evaluation planning; and the pressures applied in some cases to "push money out the door", sometimes well in advance of demonstrated need.

Why so poor?

The picture is not uniformly bleak...

While the picture is not uniformly bleak across the Commonwealth, there has been a general decline in commitment to rigorous performance measurement and evaluation across the Commonwealth, and an accompanying decline in analytical and evaluative capability. This has not been a sudden or dramatic change – rather, a gradual process of attrition and erosion over many years.

...but the problems are serious, and need to be addressed...

...with greater emphasis placed on rigorous evaluation and evidence-based policy

The causes of the problem are complex, but the symptoms are evident in many forms. Many program reviews are conducted either perfunctorily or for self-serving reasons: rigorous, relatively independent evaluation is now the exception rather than the norm. There is little evidence – least of all, perhaps, in the grants domain – of evidence-based policy formulation and review. Moreover, evaluation has been downgraded in the culture of many agencies: for example, issues of performance measurement and effectiveness do not feature strongly in the messages conveyed by Chief Executives and other departmental leaders.

What needs to be done?

Remedial action is needed on two broad fronts

Just as the decline in evaluative capacity has been a long-term and gradual process, so any remedial action will inevitably take many years to have any widespread effect. To be effective, any remedial strategy will need to take action on two broad fronts.

Effective planning is critical...

...if performance monitoring and evaluation are to be soundly based

One essential requirement is to improve the quality of planning for new grant programs. As part of new planning processes, agencies should be held responsible for ensuring that the information required for effective performance monitoring and evaluation is built into the program design. For example, there should be a clear identification of program objectives and desired outcomes; performance baselines should be established and performance indicators set; arrangements should be made for the collection and validation of key performance data; and an appropriate evaluation strategy should be designed and put in place. Finance also needs to play its part in this process – for example, by recognising that high-quality evaluation carries a cost, and is a legitimate element in the costing of a new policy proposal.

The quality and rigour of evaluation activity also must be improved...

...including in the grants domain...

Whole-of-government action is also needed to improve the quality and rigour of evaluation activity across the Commonwealth. In the grants domain specifically, an ongoing program of review and evaluation of grant programs should be put in place, designed to:

- > strengthen the base of evidence on which judgements can be made about the appropriateness, effectiveness and efficiency of grant programs;
- > critically appraise the performance of individual programs or related groups of programs; and
- > improve the overall quality of grant program spending across the Commonwealth.

...with greater openness to independent scrutiny of program efficiency and effectiveness

As a matter of good practice, agencies should plan on the basis that any ongoing grant program should be subject to a formal process of internal review at least once every five years. In the interests of rigour and transparency, also, provision should be made for some major reviews and evaluations of grant programs to be undertaken independently of the agency responsible for the programs in question.

Accounting treatment of grants

Current accounting standards offer little by way of clear guidance to grantors...

...and admit of a variety of possible interpretations...

...as illustrated recently by the different accounting treatments of the Commonwealth's health and education grants to the States

As long as current ambiguities remain, consistency, comparability and transparency will all be at risk

The Commonwealth should press the accounting standards body for speedier action to address the problem

As an interim measure, Finance should develop whole-of-government guidance on the accounting treatment of grants paid by the Commonwealth

The current accounting standards framework focuses principally on accounting from a grantee's perspective, and provides little by way of definitive guidance to grantors. Neither the accounting standards themselves nor the Generally Accepted Accounting Principles (GAAP) framework make clear in any detail how a grantor, in this case the Australian Government, should account for grants. This uncertainty has led to a variety of interpretations by different Commonwealth agencies on some key accounting issues, such as when recognition of a grant expense should occur and the appropriate accounting treatment of multi-year grants and prepayments.

Between 2003 and 2006, for example, grants payable under Commonwealth health care and education agreements with the States were accorded quite different accounting treatments, notwithstanding strong similarities in the basic structure and design of the two agreements. There was inconsistency also between the treatment of education grants in the Commonwealth's financial statements under GAAP and the treatment of those grants under the Government Finance Statistics (GFS) framework – at odds with the objective of harmonising accounting treatments between the two frameworks.

While the issues raised by this case have now been satisfactorily resolved, the current accounting standards framework remains ambiguous in some significant respects. Existing standards admit of a variety of different interpretations and accounting treatments on the part of grantors and as long as this situation prevails, the objectives of consistency, comparability and transparency will all be at risk. Clearer standards and better guidance are needed to support higher standards of consistency and transparency in accounting practices.

The Australian Accounting Standards Board (AASB) has recognised the limitations of existing accounting standards in the area of grants, but remedial action has been slow. The Commonwealth should press for speedier and more concerted action to address the current problems, both by direct representation to the AASB and through bodies such as the Financial Reporting Council and the Heads of Treasuries Accounting and Reporting Advisory Committee.

In the meantime, pending the development of any new accounting standards, Finance should develop and promulgate whole-of-government guidance, not inconsistent with the current accounting standards, on the accounting treatment of grants paid by the Commonwealth. As far as possible, the terms of this guidance should align with the ABS's treatment of grants under the GFS framework and with the terms of any new policy framework for the administration of grants.

Taxation treatment of grants

There is no 'standard' tax treatment of government grants...

...either for income tax purposes...

...or in relation to GST

Decisions on these matters need to be well-informed, and not based on questionable assumptions

Poor planning has contributed to confusion and uncertainty on taxation issues...

...with adverse consequences both for grant recipients and for government

A consideration of taxation issues should be an integral part of program planning and design...

...and undertaken in close consultation with the ATO

More helpful guidance should also be given to potential applicants and grant recipients

The taxation treatment of grants has been another area of significant confusion and uncertainty in recent times. The payment of a grant by a government agency does not have a fixed or 'standard' tax treatment for income tax purposes; rather, the treatment will depend upon a combination of factors, including the nature and characteristics of the grant (in particular, the purpose of the grant and how the grant funding is delivered), the status and circumstances of the grantee, and the provisions of any governing legislation.

Where a grant arrangement involves a taxable supply, for which the grant is consideration, a grantee registered or required to be registered for goods and services tax (GST) will be required to remit GST. The central question here is whether a grant is consideration for a supply made by the grantee. There are no provisions in the GST law relating specifically to the treatment of government grants, and as grant arrangements vary widely in their purposes, structure and the nature of the conditions they impose, no blanket statement can be made as to the 'standard' GST treatment of government grants. In some cases agencies have acted on an assumption that their grants involved a taxable supply and would therefore be subject to GST, only to discover later that this was not the case.

Improvements in program planning and design

Poor planning has been a major source of confusion on these matters. In many cases taxation issues have not been addressed at the time of the design, development and approval of a new grant program: the result has been a lack of clarity – including in publicity materials and application forms – as to whether grants are being provided on a pre-tax or post-tax basis. Grant recipients have complained to the Government when eventually it becomes clear that their grants will be subject to tax. Government in turn has come under pressure to provide additional funding to compensate for the effects of taxation on the value of the grant.

This is an unsatisfactory situation, and needs to be changed. The expected taxation treatment of a grant should be an integral part of program planning and design, rather than a matter for subsequent consideration and *post hoc* adjustment of the funding base. In future:

- > The framework for submission of new policy proposals for grant programs should require proponents to deal explicitly with taxation issues.
- > Agencies should be required to consult with the Australian Taxation Office in the process of designing a new grant program.
- > In developing their program documentation and publicity materials for a grant program, agencies should incorporate an explicit reference to the expected taxation status of the grants in question. The terms of this statement should be developed in consultation with the ATO, and include reference to the GST status of the grants and any class ruling obtained from the Commissioner of Taxation.

Taxation status of grants

Grants should be subject to taxation to the extent that they fall within the scope of general taxation law

Grants provided under Commonwealth funding programs should be subject to taxation to the extent that they fall within the scope of general taxation law. There is no strong case to exempt grants specifically from tax, as has sometimes been done in the past; instead, a better approach is to make all grants taxable, but to consider the average tax rate of likely recipients when determining the size of the grant.

Grant arrangements designed to minimise tax liability are inappropriate, and should be prohibited

It is inappropriate to structure a grant arrangement with the objective of minimising a recipient's tax obligations (as was done in one recent high-profile case). The new policy framework for the administration of grants should deal with this issue, and explicitly prohibit the structuring of grant arrangements with the objective of removing or minimising the regular tax obligations of a grantee.

'Grossing up' of grants for GST

Where relevant, agencies should 'gross up' their grants to cover the GST liabilities of grant recipients

Where consultation with the ATO indicates that a grant arrangement will be subject to GST, the administering agency should 'gross up' the value of grants paid to GST-liable grantees by 10 per cent in order to cover their expected GST liabilities and thereby provide the level of net benefit intended. Where justified on the basis of a documented risk assessment, it should also be open to an agency to pay all grants within a program on a grossed-up basis, irrespective of the GST registration status of any individual grantee.

Improving efficiency in grants administration

Too many grant programs?

There are now some 250 separate discretionary grant programs across the Commonwealth, each with its own program guidelines, advertising budget, selection and assessment procedures, funding agreements, payment and acquittal arrangements, monitoring and assessment procedures, and associated administrative costs. On the surface, at least, many of these programs appear strikingly similar in their stated purposes and intended target groups.

Time to take stock

In the haste with which many grant programs have been developed, the question has too rarely been asked as to whether an existing program could be expanded or modified to meet an identified need: rather, new programs have been added on top of existing program structures, often with little sense of overall strategy or control. It is timely to take stock of the array of grant programs now in place and, over and above any judgements made on program effectiveness, to assess the case for streamlining, simplification and rationalisation. A recent example highlights the potential value of such a process.

There are many benefits in program streamlining...

FaHCSIA has recently streamlined the structure of its community services grant programs by bringing together those programs with broadly similar purposes. As a result of this review the number of separate programs has been cut by half, from 48 to 24; program objectives and relationships have been clarified;

...as demonstrated recently by FaHCSIA

the number of performance indicators has been cut from 286 to just 62, with the quality of the remaining indicators improved; administrative and overhead savings are being made; and the resources freed by program streamlining are now being used in more productive ways – in particular, in improving the quality of service delivery and supporting the achievement of program outcomes. There is more to be done – even 24 separate grant programs catering for the community services sector is arguably too many – but the benefits are real and worthwhile.

Other agencies should follow suit

All grant-administering agencies should be encouraged to review the structure of their grant programs along similar lines, with the results to be reported in the context of the 2009–10 Budget.

There are also questions about the IT systems supporting grant programs...

There is also cause to question the efficiency of the IT system arrangements supporting the operation of Commonwealth grant programs. A Finance survey conducted early in 2006 found that there were at least 164 separate grant management systems in operation across the Commonwealth, with four agencies accounting for no fewer than 115 separate systems. There were also clear limitations on the functionality of these systems: for example, most agencies advised that they were unable to obtain consolidated management information across different grant programs without significant manual effort.

...both as to the number of such systems and their functionality

Subject to the findings of the Gershon Review...

The Gershon Review is conducting a survey of ICT expenditure and operations across FMA Act agencies, and as part of that survey, has sought detailed data on agencies' current use of grant management systems. Subject to the findings of that review, and subsequent Government decisions, Finance should lead a process designed to review and rationalise the number of grant management systems in use across the Commonwealth. The objectives should be to deliver better services, promote more consistent business processes, increase the portability of information across different systems, reduce software development and maintenance costs, and achieve administrative savings more generally. Any review should be conducted in close consultation with agencies.

...Finance should lead a process designed to rationalise the number of grant management systems in use across the Commonwealth

There is scope to eliminate unnecessary processes and cut red tape...but the first step should be to cull ineffective programs and streamline program structures

Cutting red tape

There is significant scope to improve the efficiency of grant programs by eliminating unnecessary processes and cutting red tape. The first step, however, should be to reduce the number of separate grant programs by culling redundant or ineffective programs and streamlining program structures. Apart from generating savings, this should help to clarify objectives, reduce paperwork and ease the burden of reporting and acquittal processes; to that extent, at least, it should also be welcomed by many grant recipients.

Whole-of-government processes should also be reformed

The Review has recommended a range of measures designed to improve the efficiency of whole-of-government processes for grant program administration. Examples are the replacement of the requirement for ERC consideration of detailed program guidelines with a more efficient, assurance-based process;

The needs of grant recipients should also be considered...

the abolition of the requirement to seek the Finance Minister's approval for the award of multi-year discretionary grants; and the introduction of a new and more efficient reporting system for grants, better connected to agencies' information systems. In combination, these measures should increase the efficiency of current administrative processes and, over the medium term, generate significant savings in departmental expenses.

It is important also to consider the needs and interests of grant recipients, especially those from the community and voluntary sector. A common criticism of government arrangements for the administration of grants has been the assumption that the same approach will suit all circumstances, regardless of the scale or purposes of the grant in question or the performance record of the grant recipient. The volume, detail and frequency of reporting requirements have been a particular focus of criticism in this regard.

...with greater emphasis placed on considerations of proportionality and risk

The Review accepts that there is some substance in such criticisms, and its recommendations acknowledge the need to strike a new balance, based on 'proportionality' considerations and a more measured assessment of risk. For example, where grant funding is used to support the ongoing delivery of services from the same organisations over a period of years, agencies should be encouraged to adjust the detail of their accountability and reporting requirements in line with a provider's established record of compliance and performance. These judgements will best be made at the agency level, with appropriate documentation of reasons.

Implementation strategy and transition planning

An implementation strategy and transition plan should be developed...

As the full implementation of Government decisions on this review is likely to take a number of years, an implementation strategy and transition plan should be developed which identify the appropriate staging and sequencing of particular measures. In developing this plan, priority should be given to practical measures which will improve the efficiency of current administrative processes. For example, while the Discretionary Grants Central Register will need to remain in place for the time being, as the only source of whole-of-government information on discretionary grants, reporting arrangements should be reviewed and streamlined with a view to reducing the current heavy reporting burden on agencies.

...with priority given to practical measures which will improve the efficiency of current administrative processes

Principles for reform

The problems in the grants domain stem from many sources...

...and are not confined to administrative failings alone

Remedial action is urgently needed, but comprehensive reform will take time

Some high-level principles should guide the process of reform

The problems highlighted in this report have accumulated over a number of years, and stem from a range of sources: key gaps in the whole-of-government policy framework; a lack of adequate central guidance; excessive growth in grant program numbers; poor planning; undue haste in program implementation; skill gaps within agencies; ineffective management of funding agreements; inadequate performance monitoring; and a culture which has rewarded flexibility and responsiveness over performance and effectiveness. Cultural and institutional factors have been at least as important as any failings in administrative practices as such.

Remedial action is urgently needed, and some useful steps could be taken quickly; that said, any comprehensive program of reform will inevitably take several years to have effect, especially if it is to tackle the cultural and institutional factors which lie at the heart of many of the problems.

Experience gained in the procurement area and elsewhere has demonstrated the value of establishing a set of high-level principles to help guide the process of whole-of-government reform. One general principle, common to all areas of public administration, derives from the provisions of the *Financial Management and Accountability Act 1997*: namely, that the affairs of an agency should be managed in a way that promotes the *efficient, effective and ethical use of Commonwealth resources*. More specific principles, consistent with the recommendations of this review, are set out below.

> **Robust planning and design**

High-quality planning is essential to the design of an effective and efficient grant program. There should be confidence before a program is implemented that all key planning issues have been systematically addressed and built into the program's design.

> **Outcomes orientation**

Objectives and intended outcomes should be clear from the outset. All grant programs should have a performance framework that links grant deliverables and outcomes to government priorities.

> **Collaboration and partnership**

Without detriment to other objectives, there should be a constructive and cooperative relationship between the administering agency, the grant recipient and other relevant stakeholders. Effective consultation, leading to a shared set of understandings and expectations, will help to achieve more efficient and effective grant outcomes.

> **Proportionality**

Grant programs should be ‘fit for purpose’: that is, key design features and related processes should be commensurate with the scale, nature, complexity and risks involved in the program.

> **Governance and accountability**

Grant programs should have solid governance structures and clear lines of accountability. The roles and responsibilities of Ministers, officials and other parties should be clearly established at the outset.

> **Probity and transparency**

Decisions taken on the administration of a grant program should be impartial, transparent and appropriately documented. Unless specifically agreed otherwise, competitive, merit-based selection processes should be used, based upon clearly defined selection criteria and with due attention to probity principles.

> **Value for money**

Value for money should be a prime consideration in the design and management of a grant program, including in the selection of grant recipients to deliver grant outcomes.

CONSOLIDATED LIST OF RECOMMENDATIONS

CHAPTER 2: Framework Requirements for Effective Grants Administration

Recommendation 1

The Review recommends that:

- (a) Finance develop and promulgate whole-of-government guidance covering the definitions of each major class of Commonwealth financial transaction and the principles to be applied in determining the appropriate classification of any individual transaction. The objective should be to provide better guidance to agencies in reaching their classification decisions; promote greater consistency in classification procedures and decisions across the Commonwealth as a whole; and ensure that the appropriate policy framework is applied to any given transaction, consistent with its essential characteristics;
- (b) in conjunction with its work on (a) above, Finance review the policy framework applying to each major category of Commonwealth financial transaction to ensure that it meets appropriate standards of transparency and accountability;
- (c) following implementation of the arrangements in (a) above, the framework for submission of new policy proposals should include a statement of the intended classification of a proposal against the new classification principles; and
- (d) on a progressive basis, within a timeframe set by Government, agencies should review the classification of their existing programs to ensure conformity with the new classification principles. Finance should issue guidance to agencies on the timetable and processes for this review.

Recommendation 2

The Review recommends that:

- (a) a whole-of-government policy framework be developed for the administration of grant programs across the Commonwealth;
- (b) the new grants policy framework be principles-based, with prescriptive rules and mandatory requirements kept to a minimum;
- (c) the new grants policy framework be established under the *Financial Management and Accountability Regulations 1997* in the form of guidelines issued by the Finance Minister, with a requirement that Ministers and officials performing functions in relation to the administration of grants should have regard to those guidelines, and comply with any mandatory requirements; and
- (d) in consultation with Finance, the ANAO should review and re-issue its *Better Practice Guide on Administration of Grants* to reflect the new policy framework for the administration of grants.

Recommendation 3

The Review recommends that:

- (a) at the next reasonable opportunity, and by no later than June 2009, the current FMA Regulations relating to the approval of spending proposals should be reviewed and restructured with a view to improving their logical sequence, increasing clarity, and promoting consistency of interpretation and application across FMA Act agencies; and
- (b) subject to the implementation of (a) above, Finance Circular 2008/06 should be updated and reissued to reflect the new set of FMA Regulations.

Recommendation 4

The Review recommends that Finance retain responsibility for the collection and reporting of whole-of-government information on the administration of grants, and for implementing the new reporting arrangements recommended in Chapter 4.

Recommendation 5

The Review recommends that:

- (a) Finance establish an identifiable unit within its structure to take responsibility for developing and implementing the new policy framework for grants administration and for co-ordinating action on government decisions arising from this review;
- (b) the unit established under (a) above should work collaboratively with portfolios and agencies to explain the terms of the new grants policy framework and to assist them in implementing its requirements; and
- (c) the Government provide funding for Finance to perform the functions at (a) and (b) above.

CHAPTER 3: Planning and Decision-Making Arrangements

Recommendation 6

The Review recommends that:

- (a) the framework for the planning of new grant programs should be markedly strengthened, providing greater assurance that each of the following issues has been systematically and fully addressed in program design:
 - > the strategic intent and intended outcomes of the program;
 - > expected benefits and deliverables to the Commonwealth;
 - > intended beneficiaries (as a class);
 - > program structure and design;
 - > the development of program guidelines and related documentation;
 - > stakeholder consultations (where relevant);
 - > decision-making arrangements;

- > selection criteria and selection processes;
 - > program governance arrangements;
 - > service delivery arrangements;
 - > funding agreement (form and term);
 - > payment arrangements;
 - > expected taxation treatment (based on consultation with the ATO);
 - > key performance indicators (including performance baselines and targets);
 - > monitoring, reporting and accountability arrangements;
 - > evaluation arrangements; and
 - > proposed IT platform;
- (b) any new policy proposal for the establishment of a new grant program should address each of the matters in (a) above as far as available information allows;
- (c) where the information supporting a new policy proposal is not adequate to provide the required level of planning assurance, any approval of a new grant program should be made on an in-principle basis only; in these cases, no payments should be made under the program until the responsible Minister has provided evidence that a robust planning process has been completed; and
- (d) the arrangements proposed at (a) – (c) above should replace the current requirement for ERC consideration of detailed program guidelines for a new grant program. Should additional assurance be needed in any particular case, draft program guidelines (or other suitable evidence) could be made available to ERC on request.

Recommendation 7

The Review recommends that:

- (a) decisions on the award of grants should be taken by the Minister or other approver in the portfolio or agency with functional responsibility for the program in question;
- (b) where Ministers assume the role of an approver under FMA Regulation 9, they should be required to receive and consider agency advice on the merits of grant applications, as assessed against the relevant program guidelines, before taking any decisions on the award of individual grants; this requirement should apply to all grant spending proposals, including proposals designed to satisfy commitments made in the context of an election campaign;
- (c) the advice and related briefing material provided to Ministers on grant program approvals should explicitly address the requirements of the FMA Regulations, making a clear recommendation as to what the Minister is approving and why the agency is recommending the approval;
- (d) it should be open to a Minister to reach a decision different from that recommended in an agency's advice; in such circumstances, however, or where the reasons for the Minister's decision are different from those cited in the agency's advice, there should be a requirement on the Minister to record the basis on which he or she is satisfied that a grant spending proposal represents an efficient and effective use of public money, and is in accordance with the relevant policies of the Commonwealth; and

- (e) public assurance on the integrity of decision-making in grant programs should be provided by means of a new policy framework for the administration of grants; a stronger assurance framework governing the establishment of new grant programs; greater clarity of roles and responsibilities in relation to decision-making and approval processes; stronger requirements in relation to the documentation of the reasons for decisions taken on the award of grants; and stronger disclosure and public reporting requirements.

Recommendation 8

The Review recommends that:

- (a) decisions involving the award of grants within a Minister's electorate should remain within the remit of the responsible Minister or other approver in the portfolio or agency concerned; and
- (b) should additional assurance be required in these cases, beyond the assurance mechanisms noted in Recommendation 7(e), portfolio Ministers who are members of the House of Representatives could be required to report periodically to the Finance Minister on decisions they take involving grants in their own electorate, together with a summary statement of their reasons for those decisions.

Recommendation 9

The Review recommends that the FMA Regulations authorising the terms of a new grants policy framework require all approvers of grant spending proposals under FMA Regulation 9 to record in a document the *basis* on which the approver is satisfied that the proposed expenditure represents an efficient and effective use of public money, and is in accordance with the relevant policies of the Commonwealth.

Recommendation 10

The Review recommends that:

- (a) the requirement on Ministers to seek the Finance Minister's approval for the award of certain multi-year discretionary grants be abolished; and
- (b) should specific or additional controls need to be placed on the forward commitment of funds for expenditure on multi-year discretionary grants, this be achieved by placing specific limitations on the delegation of the Finance Minister's powers under FMA Regulation 10.

Recommendation 11

The Review recommends that:

- (a) should a Minister wish to have the flexibility to provide grant funding outside of regular program guidelines and processes, this intention should be made transparent in the design of a new grant program and authorised specifically in the terms of Cabinet's approval of a new policy proposal;
- (b) any limits on a Minister's powers to exercise the flexibility under (a) above should be clearly specified in the terms of the Cabinet's approval; and
- (c) Ministers and agencies should review their existing programs to identify any programs in which Ministers may wish to provide grant funding outside of established program guidelines and processes; the results of this review should be reported for Cabinet's consideration in the context of the 2009–10 Budget.

CHAPTER 4: Disclosure and Reporting Arrangements

Recommendation 12

The Review recommends that a new reporting system be developed to meet whole-of-government requirements for information on grants, along with a range of public information, transparency and accountability objectives. The new reporting system should:

- (a) be developed in close consultation with agencies, and well connected to agency information systems;
- (b) be comprehensive in its coverage, covering all grant programs and details of all grants awarded (within a defined scope);
- (c) provide online public access to information on Commonwealth grant programs (i.e., the availability of grants), forthcoming grant selection processes, and details of grants awarded (with links to more detailed information on agency websites);
- (d) require agencies to lodge details of any grant awarded within two weeks of the signing of the funding agreement for the grant in question;
- (e) be designed to meet the full range of whole-of-government reporting requirements relating to grants, including Annual Report requirements, ERC reporting requirements (on discretionary grants) and Senate Order 192 requirements, as well as agency-specific requirements as far as possible;
- (f) have a high level of functionality and analytical capability, including a range of tailored reporting tools;
- (g) be based upon strong data quality standards and data entry protocols, supported by effective quality assurance procedures; and
- (h) have regard to experience gained with the operation of AusTender reporting system for procurement reporting, and be compatible with the design of that system as far as practicable.

Recommendation 13

The Review recommends that the Australian National Audit Office be invited to conduct an audit of the new reporting system proposed in Recommendation 12. The audit should be conducted in two stages: the first at the detailed design stage, before full implementation, to provide assurance that the system is structured appropriately, in accordance with its intended objectives; and the second at the post-implementation stage, to provide assurance that the new system is operating efficiently and effectively.

Recommendation 14

The Review recommends that, subject to the findings of the audit report proposed in Recommendation 13, and once there is adequate assurance that the new reporting system is operating efficiently and effectively:

- (a) the *Discretionary Grants Central Register* be decommissioned and dismantled, noting that the information currently collected for purposes of the Register would be fully captured by the new reporting system;
- (b) the *GrantsLink* managed by Infrastructure be decommissioned as a whole-of-government reporting system on grants;
- (c) whole-of-government reporting requirements in relation to grants be reviewed and rationalised, having regard to the information made available under the new reporting system; and
- (d) the Senate be encouraged to review the operation of, and continuing need for, Senate Order 192.

CHAPTER 5: Funding Agreements for Grants

Recommendation 15

The Review recommends that:

- (a) funding agreements for grants should be designed to protect the Commonwealth's interests by ensuring that public money is used for its intended purposes; and
- (b) funding agreements should be structured on the assumption that the conditions attaching to a grant are both obligatory and enforceable, and that funds will be recovered, or other remedies applied, in the event of any breach of those conditions.

Recommendation 16

The Review recommends that:

- (a) the funding agreement used in relation to any particular grant should be based upon considerations of 'proportionality': that is, it should be tailored to reflect factors such as the objectives of the program, the scale and complexity of the grant in question, the context in which the grant is made, the length of funding involved, the desired structure of payments, the conditions attaching to the grant, the nature and level of risks involved, and the desired remedies for non-compliance;
- (b) without compromising the principles of enforceability and proportionality, funding agreements should be cast in plain English as far as possible, with a minimum of complexity and legal jargon;
- (c) as part of a new policy framework for the administration of grants, Finance should produce a checklist of issues to be considered in the development of a funding agreement, leaving agencies to make detailed decisions in the context of their particular program circumstances and needs.

Recommendation 17

The Review recommends that, consistent with proportionality considerations:

- (a) funding agreements for small-scale, one-off grants should generally take the form of a simple letter of offer (having regard, in the drafting of any such letter, to the elements of contract formation and considerations of enforceability);
- (b) contracts be used in the case of large-scale or complex grants, such as grants for the funding of major infrastructure projects involving high levels of conditionality and multiple funding partners;
- (c) deeds be recognised and promoted as a legitimate form of funding agreement, especially in the case of medium-sized grants or in circumstances in which there may be room for doubt as to the enforceability of a contract (for example, due to a lack of consideration or a lack of intention to create legal relations); and
- (d) in consultation with the ANAO, Finance arrange for guidance to be provided to agencies on the use of deeds as funding agreements, and the circumstances in which the use of deeds may be appropriate.

CHAPTER 6: Performance Measurement and Assessment

Recommendation 18

The Review recommends that:

- (a) as part of the planning process for a new grant program, agencies should be held responsible for ensuring that the information required for effective performance monitoring and evaluation is built into program design: in particular, that there is a clear identification of program objectives and desired outcomes, both intermediate and final; that performance baselines are established, and performance indicators set, both at the program and project level; that key performance data are collected and validated; and that an appropriate evaluation strategy is designed and put in place, with a clear indication of stages, timelines and responsibilities;
- (b) beyond the immediate work of the Expenditure Review Taskforce, an ongoing program of review and evaluation of grant programs be put in place. This program should be designed to strengthen the base of evidence on which judgements can be made about the effectiveness and efficiency of grant programs; critically appraise the performance of individual programs or related groups of programs; and improve the overall quality of grant program spending across the Commonwealth;
- (c) in the interests of rigour and transparency, some of the major reviews and evaluations to be conducted under the program at (b) above should be undertaken independently of the agency responsible for administering the grant program or programs in question; and
- (d) more broadly, the Government consider measures designed to improve the quality and rigour of evaluation activity across the Commonwealth; to increase the capacity for high-quality and independent evaluation; and to promote a culture more conducive to independent scrutiny of program efficiency and effectiveness.

CHAPTER 7: Accounting Treatment of Grants

Recommendation 19

The Review recommends that:

- (a) through mechanisms such as the Financial Reporting Council, the Heads of Treasuries Accounting and Reporting Advisory Committee and direct representation, the Commonwealth should encourage the Australian Accounting Standards Board to expedite its review of the relevant Australian accounting standards with a view to clarifying the accounting treatment of grants, especially from the grantor's perspective;
- (b) pending the development of any new accounting standards, Finance should develop whole-of-government guidance, not inconsistent with the current accounting standards, on the accounting treatment of grants paid by the Commonwealth. As far as possible, the terms of this guidance should align with the ABS's treatment of grants under the GFS framework and with the terms of any new policy framework for the administration of grants. Once finalised, this guidance should be promulgated in an authoritative form, such as a Finance Minister's Order.

CHAPTER 8: Taxation Treatment of Grants

Recommendation 20

The Review recommends that:

- (a) the expected tax treatment of grants should be a matter for explicit consideration in the planning and design of any new grant funding program. The framework for submission of new policy proposals for grant programs should require proponents to deal explicitly with taxation issues, and the terms of any government announcements on new grant programs should include a reference to the expected taxation treatment of the grants;
- (b) agencies should be required to consult with the Australian Taxation Office in the process of designing a new grant program. The objective would be to provide additional certainty regarding the expected taxation treatment of grants, and more helpful guidance to potential applicants and grant recipients;
- (c) in developing their program documentation and publicity materials for a grant program, agencies should incorporate an explicit reference to the expected taxation status of the grants in question. The terms of this statement should be developed in consultation with the ATO, and include reference to the GST status of the grants and any class ruling obtained from the Commissioner of Taxation; and
- (d) Finance should work with the ATO to ensure that agency requests for advice on the taxation treatment of grant programs can be processed promptly and efficiently.

Recommendation 21

The Review recommends that, as a matter of general principle and standard practice, grants provided under Commonwealth funding programs should be subject to taxation to the extent that they fall within the scope of general taxation law. Where tax is potentially payable on a grant, the new policy framework for the administration of grants should explicitly prohibit the structuring of grant arrangements with the objective of removing or minimising the regular tax obligations of a recipient.

Recommendation 22

The Review recommends that, where consultation with the ATO indicates that a grant arrangement will be subject to GST, the administering agency should 'gross up' the value of grants paid to GST-liable grantees by 10 per cent in order to cover their GST liabilities and thereby provide the level of net benefit intended. Where justified on the basis of a documented risk assessment, it should be open to an agency to pay all grants within a program on a grossed-up basis, irrespective of the GST registration status of any individual grantee.

CHAPTER 9: Improving Efficiency in Grants Administration

Recommendation 23

The Review recommends that:

- (a) grant-administering agencies be encouraged to review the structure of their grant programs with a view to reducing the overall number of programs, achieving greater coherence and clarity of objectives, improving transparency, reducing but sharpening the range of performance indicators, and achieving administrative savings; and
- (b) agencies be asked to report on the results of the review at (a) in the context of the 2009–10 Budget.

Recommendation 24

The Review recommends that, subject to Government decisions on the findings of the Gershon Review:

- (a) the number of grant management systems in use across the Commonwealth be reviewed and rationalised with a view to delivering better services, promoting consistent business processes, increasing the portability of information across different systems, reducing software development and maintenance costs, and improving efficiency more generally;
- (b) the review recommended at (a) should be led by Finance but conducted in close consultation with agencies;
- (c) as a first step, Finance should work in partnership with relevant line agencies, through the Business Process Transformation Committee, to determine standard business process patterns for grants management across agencies; and
- (d) in the longer term, the objective should be to authorise a small number of software platforms which meet most, if not all, the grant management system requirements of Commonwealth agencies; within this set, agencies should be free to choose the particular program best suited to their needs, with some flexibility also to adapt the platform chosen to meet particular agency business requirements.

Recommendation 25

The Review recommends that, once Government decisions have been taken on the outcomes of this review:

- (a) Finance develop and circulate to agencies an implementation strategy and accompanying transition plan;
- (b) in developing the transition plan at (a) above, priority be given to practical measures which will improve the efficiency of current administrative processes, both at whole-of-government level and within particular agencies; and
- (c) as one transitional measure, Finance review the details of its current reporting requirements in relation to the Discretionary Grants Central Register, with a view to improving efficiency and reducing the reporting burden on agencies.

Recommendation 26

The Review recommends that, where grant funding is used to support the ongoing delivery of services from the same organisations over a period of years, agencies should be encouraged to adjust the detail of their accountability and reporting requirements in line with a provider's established record of compliance and performance. Subject to transparency considerations and risk management principles, service providers with consistent records of high performance and reliability should be able to 'earn' lighter-touch accountability and a greater measure of autonomy, relative to other providers without an established record of performance.

01

CHAPTER ONE: INTRODUCTION



The Government has commissioned a comprehensive strategic review of the administration of Australian Government grant programs, to be managed by the Department of Finance and Deregulation (Finance). The objective of the review is to improve efficiency, effectiveness, accountability and transparency in the administration of grant programs across the Commonwealth.

The review comprises two distinct but related elements. The first element has a 'framework' focus, requiring an examination of the current policy framework and related administrative processes for the management of Australian Government grant programs. The second element focuses principally on issues of appropriateness and effectiveness, involving an assessment of the merits of discretionary grants as a vehicle for delivering government policy objectives. Detailed terms of reference covering both elements of the review are provided at [Attachment A](#).

This report addresses the first element of the review, and makes a series of recommendations for improvements to the current policy framework for the administration of grants. A separate report on the second element of the review is due to be provided by mid-August 2008.

Commonwealth grant programs: scale and characteristics

There is no single, comprehensive source of data on the number of individual grant programs, the number of grants awarded or the total scale of grant program funding across the Commonwealth. Data need to be compiled from a number of different sources, and even then, a significant element of estimation is necessary. Issues of scope and definition also arise.

According to the Discretionary Grants Central Register (DGCR), managed by Finance, over 49,000 individual 'discretionary grants' were approved in calendar year 2007 under some 250 separate funding programs, involving total expenditure of more than \$4.5 billion.¹ In addition, more than 90 different Commonwealth specific purpose payments (SPPs) are currently made on a conditional basis to State, Territory and local governments, principally in the form of legislated 'grants'.² Total SPP payments to the States and Territories in 2007–08, including payments made 'through' the States and directly to local government, are estimated at some \$32.1 billion.³ Taking both these funding sources in combination, and allowing for other conditional grant programs not included within the scope of these aggregates⁴, current Commonwealth expenditure on all forms of conditional grants is likely to be between \$40 billion and \$50 billion annually, or about one-sixth of total Commonwealth outlays.⁵

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- 1 These estimates understate the total volume of 'discretionary grants' activity, in that a relatively wide range of grant programs have been exempted from reporting on the DGCR. Exemptions include programs involving grants to educational institutions and medical research organisations; emergency payment programs; payments to overseas aid organisations; grants made under commercial industry development programs; payments made to State and Territory governments; and arrangements involving 'service agreements' between the Commonwealth and service providers.
 - 2 In the constitutional sense of the term. Section 96 of the Constitution (the 'grants power') provides that: "During a period of ten years after the establishment of the Commonwealth and thereafter until the Commonwealth otherwise provides, the Parliament may grant financial assistance to any State on such terms and conditions as the Parliament thinks fit."
 - 3 Source: *Budget Paper No. 3, 2008-09*, Table 3.1
 - 4 For example, grants for higher education under the *Higher Education Support Act 2003*. As these grants are not passed 'to' or 'through' the States, but rather go directly to higher education institutions, they are not classified as specific purpose payments.
 - 5 This estimate rises sharply if unconditional (or 'untied') grant payments are included; for example, GST grant payments to the States and Territories in 2007–08 amounted to \$42.6 billion. The focus of this report, however, is on conditional grants: that is, grants which are paid subject to defined and enforceable conditions, and which can be withheld, or are potentially recoverable, in the event that those conditions are not met.

Such an aggregate figure masks the significant diversity in the nature and characteristics of grant programs across the Commonwealth. To illustrate the point:

- > Some grant programs are covered by legislation or regulations which allow little or no discretion as to who is to be paid, for what amount, or on what terms. In other cases, by contrast, there is a wide degree of discretion exercised by Ministers or other decision-makers in these respects.
- > Some programs provide short-term, one-off support or assistance to grant recipients, with only a broad specification of purposes and quite loose accountability requirements. Other programs are project-based, with duration linked to the length of the project and a much tighter specification of deliverables. Other programs again support the ongoing delivery of services, with funding provided to the same or similar organisations more or less continuously over a period of years.
- > Many programs are contestable in their design, with applications assessed against a defined set of selection criteria and ranked in order of merit. Other programs, however, are non-contestable – either because the grant recipients are predetermined (for example, specified in legislation), or because applications are individually assessed against selection criteria rather than comparatively assessed against other applications.⁶

Grant programs vary widely also in their scale and degree of complexity. Some take the form of simple grants for small amounts to community organisations; others involve large-scale funding for complex projects – for example, major infrastructure projects with elaborate governance structures and multiple funding partners. Likewise, there are wide variations from program to program in planning and decision-making procedures, administrative arrangements, level of conditionality, the forms and terms of funding agreements, and in the quality and rigour of performance monitoring and evaluation arrangements. For these reasons, and others, it is extremely difficult to generalise in the grants domain: for every general observation made, there will inevitably be some significant exceptions.

Even within the sub-set of grants classified as ‘discretionary’⁷, diversity rather than uniformity is the norm. According to DGCR data for 2007, the value of grants approved in that year ranged from less than \$100 (in the case of some small community grants) to \$408 million (for a large water recycling project). Most grants approved (63 per cent) were for amounts of less than \$5,000, with a small number only (118) in excess of \$5 million; reflecting this, the median size of grant was less than \$3,000, whereas the average grant size was close to \$93,000. Two programs accounted for nearly half of all discretionary grants awarded in 2007.⁸

Major recipients of discretionary grants in 2007 were community organisations (51.0 per cent of all grants) and educational institutions (20.4 per cent of grants); however, government organisations, Indigenous organisations, sports-related bodies and for-profit organisations were also significant beneficiaries. The average value of grants varied significantly according to the category of recipient involved: for example, Indigenous organisations attracted just 5.6 per cent of grants awarded, but 22.3 per cent of total funding approved; by contrast, educational institutions received 20.4 per cent of grants awarded, but only 3.6 per cent of total funding approved.

6 The former *Regional Partnerships Program* was an example of a non-legislated, non-contestable grants program.

7 Finance defines discretionary grants as “payments where the Portfolio Minister or paying agency has discretion in determining whether or not a particular agency receives funding and whether to impose conditions in return for the grant.” (DGCR User Manual, November 2006)

8 Namely, the *Volunteer Small Equipment Grants Program*, managed by the Families, Housing, Community Services and Indigenous Affairs portfolio (12,006 grants, to a total value of \$27.3 million); and the *Active After-school Communities Program*, now managed by the Health and Ageing portfolio (12,108 grants, to a total value of \$22.9 million).

Attachment B provides more detailed data on the scale and distribution of discretionary grant funding approved in 2007.

According to data from the DGCR, both the number and value of discretionary grants awarded have grown strongly in recent years – from less than 4,000 grants with a total value of about \$580 million in calendar year 2000 to around 49,000 grants with a total value of \$4.5 billion in calendar 2007 (Table 1.1).

Some part of this growth can be attributed to changes over time in the scope and coverage of the Register itself; for example, grants awarded under Indigenous funding programs were not required to be reported prior to 1 July 2005, and a significant number of small-value sporting grants administered by the Australian Sports Commission were not reported at all before 2007.⁹ Even allowing for these factors, however, it seems clear that there has been substantial growth in the overall scale of discretionary grants activity, especially since 2004: between 2006 and 2007, for example, the number of discretionary grants reported more than doubled, and the total value of funding approved grew by more than 60 per cent, on a like-to-like basis.

Table 1.1: Number and value of Commonwealth discretionary grants, 2000 to 2007

Calendar year	Number of grants awarded	Value of grants approved (\$m)
2000	3,941	579.5
2001	5,388	660.1
2002	6,141	451.1
2003	7,459	494.1
2004	12,006	729.5
2005	12,161	1,901.4
2006	14,359	2,715.5
2007	49,060	4,549.9

Source: Discretionary Grants Central Register. Data are not strictly comparable over time (see the comments below).

Policy context for the review

The administration of Commonwealth grant programs has been the subject of significant audit activity, and related parliamentary scrutiny, in recent years.

The Australian National Audit Office (ANAO) has conducted more than twenty performance audits of grant programs since 2004–05 (Attachment C). Many of these reports have raised significant issues going both to the overall framework for the administration of grant programs and the quality of administration of individual programs within particular agencies. The ANAO has highlighted the fact

⁹ There were about 8,000 such grants in calendar 2006, to an estimated value of around \$15 million. Data quality issues relating to the Discretionary Grants Central Register are further discussed in Chapter 4.

that the administration of grant funding is an important and sensitive area of public administration, requiring care on the part of agencies and Ministers, where relevant, to ensure that programs are administered in accordance with legislative provisions and the program parameters determined by government.¹⁰

In a number of the cases examined in the course of its performance audits, the ANAO has concluded that the relevant agency's administration of a grant program has fallen short of an acceptable standard of public administration. Major issues and criticisms raised in its reports have included deficiencies in the application of the financial framework governing the expenditure of public money; weaknesses in program planning, design and decision-making processes; deficiencies in program guidelines; flaws in procedures for selecting grant recipients and successful projects, and for announcing the terms of grant approvals; a lack of effective documentation, especially of the reasons for key decisions; weaknesses in grant agreements, including a lack of clarity as to the roles and responsibilities of different parties; a lack of effective oversight of funded projects; and weaknesses in performance monitoring, evaluation and accountability arrangements.

It is fair to note that many of these issues are not entirely new; indeed, many of the same issues were raised in a key report of a House of Representatives Committee in 1994.¹¹ It is fair to note also that, at least in the judgment of the Review, many of the ANAO's criticisms derive as much from weaknesses in the whole-of-government framework governing the administration of grant programs as from poor administration on the part of the agency or agencies concerned.

In responding to the issues raised in the ANAO's audit reports, many agencies have acted promptly to improve the administration of their grant programs. Specific reforms have included the review of guidelines for the administration of grant programs; the introduction of portfolio-wide systems, tools and procedures for the development and management of grant programs; and the re-engineering of business processes with a view to supporting greater efficiency, effectiveness, consistency and accountability in grants administration. Some agencies are well advanced in their work on such reforms, and have already implemented significant changes; others, while committed in principle to reform, are still at an early stage of implementation.

The new Government has made strong commitments to improve standards of transparency and accountability in public administration generally, and to ensure that policy making is soundly evidence-based.¹² The review team has been mindful of these commitments in undertaking its work and developing its recommendations.

Definitional and scoping issues

The review's terms of reference define grants as "non-reciprocal transfers of resources from the Australian Government to other entities which may or may not be subject to unilaterally imposed conditions". In practice, however, this definition is only one of many in force across the Commonwealth:

10 Australian National Audit Office, *Audit Focus* newsletter, December 2007

11 House of Representatives Standing Committee on Environment, Recreation and the Arts, *The Community, Cultural, Recreational and Sporting Facilities Programme: a review of a report on an efficiency audit by the Auditor-General*, 1994

12 See, for example, The Hon. Kevin Rudd MP, Prime Minister of Australia, *Address to Heads of Agencies and Members of the Senior Executive Service*, Great Hall, Parliament House, Canberra, 30 April 2008, and The Hon. Lindsay Tanner MP, Minister for Finance and Deregulation, *Government to improve the transparency and accountability of Public Service programs and funding*, Media Release 16/2008, 13 May 2008

there is no common understanding across agencies as to what is meant by a 'grant' or 'grant program', and many of the definitions currently in place are at odds with the common meaning of terms.¹³

The lack of common terminology and any standard definitional framework has been evident throughout the course of the review. In the interests of promoting greater consistency in this respect, the Review has recommended (in Chapter 2) that Finance should promulgate whole-of-government guidance on the definitions of each major class of Commonwealth financial transaction, including grants, and the principles to be applied in determining the appropriate classification of any individual transaction. For purposes of its own work, the Review has adopted the assumption that, while the terms and conditions attaching to a grant may vary widely from program to program, some degree of conditionality will always be present: on this view, a transfer of resources from government to another entity with no element of conditionality attached would not be a 'grant', but a 'gift'.

An important scoping issue for the review was the extent to which its considerations should encompass the wide range of Commonwealth specific purpose payments mentioned above. While recognising that many SPP payments can legitimately be argued to be grants, in the broadest sense of that term, the Review formed the view that it should focus its attention principally on the set of (non-SPP) grant programs commonly described as 'discretionary grants'. There were two main reasons for this choice: firstly, that most of the issues which had given rise to the commissioning of the review had arisen in the sphere of discretionary grants, rather than SPPs; and secondly, that SPPs are currently subject to a separate process of review and reform as part of the new framework for federal financial relations agreed by the Council of Australian Governments (COAG).¹⁴ The Review consulted on this matter both with Treasury, which is managing the process of SPP reform, and with the consultative group for the review. Both were comfortable with the approach adopted.

Unless otherwise stated, the recommendations provided in this report relate to 'discretionary grant' programs which are conditional in nature but are outside the scope of the current SPP reform process. That said, most of the key principles underlying the recommendations apply equally to many SPP grant programs, subject only to any specific provisions which may be contained in a program's governing legislation.

Conduct of the review

A review team was established in early March 2008. The team comprised an independent leader with previous APS experience and three current APS senior officers with experience in financial management, grants policy and administration.¹⁵ Support services were provided by the Reviews and Training Branch in Finance, which also managed administrative processes relating to the review.

A consultative group was established by Finance to discuss issues raised by the review and more generally to provide input to the review process. The consultative group, which met on three occasions, included representatives from Finance (chair), the Department of the Prime Minister and Cabinet (PM&C), Treasury, the Department of Families, Housing, Community Services and Indigenous Affairs (FaHCSIA), the Department of Infrastructure, Transport, Regional Development and Local Government

13 For example, one agency draws a distinction between a 'grant' and a 'funding agreement', defining a grant as "A gift from the crown, which may be subject to conditions. A grant does not involve an agreement between the parties."

14 See *Budget Paper No. 3, 2008–09*, Parts 2 and 3

15 The team comprised two senior officers from Finance and one seconded from a line agency (FaHCSIA) with major grants administration responsibilities.

(Infrastructure) and the Australian Research Council (ARC). In addition, the review team consulted widely within Finance; held a number of bilateral meetings with the ANAO, Treasury and several line agencies; conducted a workshop with representatives of the six largest grant-administering agencies within the Commonwealth¹⁶; met with the Chief Financial Officer Forum; and conducted informal consultations with officers from a wide range of agencies.

Structure of the report

The report follows closely the structure of the terms of reference for the first element of the review. In summary:

Chapter 2 deals with the whole-of-government framework for grants administration across the Commonwealth. It highlights some key respects in which the current framework is deficient, and needs to be reformed.

Chapter 3 deals with planning and decision-making issues in grants administration, including the roles and responsibilities of Ministers and other decision-makers. It highlights the importance of effective planning and design of grant programs, and proposes a number of significant changes to the current decision-making framework.

Chapter 4 deals with disclosure and reporting issues. It finds that current arrangements for whole-of-government reporting on grants are of poor quality, inefficient and lacking in transparency. It argues that a new reporting system is needed to meet whole-of-government requirements for information on grants, along with a range of public information, transparency and accountability objectives.

Chapter 5 deals with funding agreements for grants. It highlights the need for the conditions attaching to grants to be legally enforceable, as a means of ensuring that public money appropriated for grants is used for its intended purposes. It argues that funding agreements should be tailored to reflect the nature of the program in question, the conditions attaching to the grant and the nature and level of risks involved. The chapter outlines the circumstances in which particular forms of funding agreement might appropriately be used.

Chapter 6 deals with performance measurement and assessment issues. It highlights some major deficiencies in the quality of performance measurement across the Commonwealth, and raises questions about the likely effectiveness of some grant program spending. It proposes an ongoing program of review and evaluation of grant programs, but with a stronger emphasis on independent program evaluation. More broadly, it suggests that the Commonwealth should increase its capacity for high-quality and rigorous evaluation, and promote a culture more conducive to the independent scrutiny of program efficiency and effectiveness.

Chapter 7 deals with the accounting treatment of grants. It highlights some gaps and ambiguities in the current accounting standards framework, noting that these have led to different interpretations of the standards by different agencies. It proposes action, both short-term and longer-term, to improve consistency in the accounting treatment of Commonwealth grants.

16 The workshop was held on 15 May 2008. Participating agencies, in addition to Finance, were FaHCSIA; Infrastructure; the Department of Health and Ageing; the Department of Environment, Water, Heritage and the Arts (DEWHA); the Department of Education, Employment and Workplace Relations (DEEWR); and the Department of Innovation, Industry, Science and Research (Innovation).

Chapter 8 deals with the taxation treatment of grants. It notes the confusion and problems which have arisen in this area, stemming largely from the fact that taxation issues have often been treated as an after-thought rather than as an integral part of program design. The chapter recommends a number of measures designed to address this issue. It also deals with the taxation status of grants more generally, including arrangements for the 'grossing up' of grants for GST.

Chapter 9 deals with a range of efficiency issues related to the administration of grant programs. It argues that there are too many separate grant programs operating across the Commonwealth, and proposes a number of measures designed to streamline program structures, reduce unnecessary burdens on grant recipients and cut red tape. The chapter also recommends that the large number of grant management systems in use across the Commonwealth be reviewed and rationalised with a view to delivering better services, reducing costs and improving efficiency.

An **Executive Summary** provides an overview of key findings of the review, together with a consolidated set of recommendations.

02

CHAPTER TWO: FRAMEWORK REQUIREMENTS FOR EFFECTIVE GRANTS ADMINISTRATION



This chapter examines the adequacy of the whole-of-government framework for the administration of grants. It concludes that there are some key gaps and weaknesses in the existing framework, and that significant changes will be needed to support greater efficiency, effectiveness, accountability and transparency in grants administration. The chapter makes a number of specific recommendations for change.

Framework requirements for effective grants administration

The Review has identified four principal ‘framework’ requirements which need to be in place in order to support the effective administration of grants across the Commonwealth. These are:

- a standard framework of concepts, definitions and classification principles, providing a common understanding of the meaning of terms and a clear basis for the interpretation and application of policy guidance;
- a clear framework of policy principles governing the administration of grant programs across the Commonwealth;
- a strong financial management framework, with clear links drawn between the requirements of that framework and the responsibilities of decision-makers and others involved in the administration of grant programs; and
- a robust framework for the collection and reporting of statistical and other information on Commonwealth grants, designed to meet both administrative requirements and public accountability objectives.

There are some important connections between these different framework elements. For example, any whole-of-government statement of policy principles would require a common language of communication across agencies if it is to be understood and consistently interpreted. Likewise, any system of data collection and reporting would be effective only if there were a supporting framework of definitions and classification principles which reporting agencies had adopted and applied.

The Review considers that there are some important gaps and weaknesses in each of the respects just identified. No whole-of-government framework is currently in place in two of the areas mentioned (namely, concepts, definitions and classification principles; and policy principles for grants administration). A strong financial management framework already exists across the Commonwealth, but its application in the grants program environment has been a source of considerable uncertainty and confusion. The system currently used for the collection of whole-of-government information on ‘discretionary grants’ is inefficient in its design and poorly regarded by agencies; more seriously, it fails to meet either its own stated purposes or wider public accountability objectives.

The evidence supporting the Review’s conclusions on these matters is summarised below. Additional evidence, including more detailed information on particular issues, is provided in subsequent chapters.

(a) Concepts, definitions and classification principles

As noted in Chapter 1, a fundamental gap in the current framework for grants administration is the lack of any standard framework of definitions and classifications. For example, there is no common understanding across the Commonwealth as to what exactly constitutes a ‘grant’ or a ‘grant program’.

There is little clarity, let alone consensus, as to what key features should distinguish a 'grant' from a 'gift', 'procurement' or other form of financial transaction. Widespread inconsistency and potential for confusion is the result.

In the absence of any whole-of-government guidance in these respects, individual agencies have created their own definitions and classification systems. The nature of these systems varies widely, from collections of definitions issued by means of Chief Executive Instructions or other agency guidelines to highly structured systems for determining the status and classification of a particular financial arrangement.¹⁷ Different agencies have adopted different classification practices and, to some extent, different classification cultures.¹⁸ On the border between grants and procurement, for example, some have chosen to err on the side of procurements rather than grants, whereas others have opted the other way. Convenience rather than principle has often been at work: for example, some agencies have openly acknowledged that a factor underlying their large number of grant programs has been a wish to avoid the application of the Commonwealth Procurement Guidelines. There is no effective mechanism of central oversight or scrutiny of agencies' decisions in these respects.

Even basic terminology is a major area of inconsistency. Across agencies, the same terms are used with widely different meanings, and different terms to describe the same underlying concept. A term such as 'funding agreement', for example, is used in a wide variety of senses: in some cases, as a general term to describe an agreement between the Commonwealth and other parties to a financial arrangement; in other cases, in a highly particular sense, effectively as a synonym for 'grant'. As was evident at the agency workshop mentioned in Chapter 1, it is extremely difficult to conduct an effective conversation on grant-related issues in the face of such wide variations in the meaning and interpretation of terms.

These problems are by no means confined to Commonwealth Government administration, or indeed to Australia.¹⁹ That said, they represent a significant barrier in the way of any whole-of-government effort to improve the quality of grants administration across the Commonwealth, and therefore need to be addressed.

The Review's major conclusion in this area is that, in the interests of promoting greater clarity and consistency across the Commonwealth, Finance should issue overarching, whole-of-government guidance covering the definitions of each major class of Commonwealth financial transaction, including grants, and the principles to be applied in determining the appropriate classification of any individual transaction. The principles should focus upon issues of substance and essential characteristics, rather than incidental features (such as program name or funding source). The aim should be to provide better guidance to agencies in reaching their classification decisions; promote greater consistency in classification procedures across the Commonwealth as a whole; and ensure that the appropriate policy framework is applied to any given transaction, consistent with its essential characteristics.

On the basis of its own examination of these issues, the Review has identified seven broad classes of financial transaction which might be identified in any such whole-of-government guidance. The seven categories, along with their working draft definitions, are as follows:

17 An example of the latter is the Procurement Funding Tree developed by the Department of Education, Employment and Workplace Relations (DEEWR).

18 In some cases, programs transferred between portfolios as a result of Machinery of Government changes have changed in their classification status (e.g., from grant to procurement), without any material change in their essential characteristics.

19 See, for example, *Working with the Third Sector*, National Audit Office, United Kingdom, 2005 and *Improving financial relationships with the third sector: Guidance to funders and purchasers*, HM Treasury, United Kingdom, May 2006 (Chapter 2)

Grant: A *grant* is a conditional transfer of resources from the Australian Government to a recipient for a specified purpose. Grants are directed to assisting recipients to achieve their own goals whilst also supporting Australian Government policy.

Procurement: A *procurement* is an arrangement for the acquisition of goods or services by or on behalf of the Australian Government in accordance with the *Commonwealth Procurement Guidelines*.

Investment: An *investment* is a financial transaction that involves the purchase of an asset for the primary purpose of earning income or a profitable return for the Australian Government.

Loan: A *loan* is a financial transaction under which the Australian Government advances a sum of money to a borrower in consideration of the borrower agreeing to repay that sum on a future date or on demand.

Gift: A *gift* is an unconditional transfer of resources from the Australian Government to another party.

Entitlement: An *entitlement* is a transfer payment authorised by legislation or by an executive decision of Government and payable in accordance with defined eligibility criteria to a specified person, class or entity.²⁰

Compensatory payment: A *compensatory payment* is a payment designed to compensate individuals for financial losses or other adverse consequences caused by a decision, action or omission on the part of the Australian Government.²¹

The Review accepts that these definitions, and the classification structure on which they are based, would need to be subject to further consideration and development before any whole-of-government guidance could be issued. In particular, more work would be needed to develop clear classification criteria and principles: that is, to identify the key characteristics which should be used to distinguish between the various categories of Commonwealth financial transaction. It would be important also to ensure that each of the broad categories of transaction is covered by a robust policy framework, meeting suitable standards of transparency and accountability.

The Review sees considerable benefit in having any whole-of-government guidance on these matters encompass the full range of Commonwealth financial transactions rather than being limited, for example, to grants alone. The reason for this is that many of the most problematic issues in this area arise at the boundaries between different transactions – in particular between grants and procurements but also, for example, between grants and loans and grants and gifts – and much clearer guidance is needed to inform agencies' classification decisions in these marginal cases.

Once a standard set of definitions and classifications has been developed and put in place across the Commonwealth, the Review considers that the framework for submission of new policy proposals to ERC or Cabinet should include a statement of the intended classification of an NPP against the new classification principles (and hence of the relevant policy framework intended to apply). Progressively, also, within a timeframe set by Government, agencies should review the classification of their existing programs to ensure conformity with the new classification principles. Finance should issue guidance to agencies on the timetable and processes for this review.

20 Examples of entitlements are income support payments, aged care pensions and salaries paid to Commonwealth employees.

21 Examples are the act of grace payments made under the *Financial Management and Accountability Act 1997*, payments made under the *Scheme for Compensation for Detriment Caused by Defective Administration* (CDDA Scheme), and in the case of Australian Public Service employees, compensation payments made under the *Public Service Act 1999*.

Recommendation 1

The Review recommends that:

- (a) Finance develop and promulgate whole-of-government guidance covering the definitions of each major class of Commonwealth financial transaction and the principles to be applied in determining the appropriate classification of any individual transaction. The objective should be to provide better guidance to agencies in reaching their classification decisions; promote greater consistency in classification procedures and decisions across the Commonwealth as a whole; and ensure that the appropriate policy framework is applied to any given transaction, consistent with its essential characteristics;
- (b) in conjunction with its work on (a) above, Finance review the policy framework applying to each major category of Commonwealth financial transaction to ensure that it meets appropriate standards of transparency and accountability;
- (c) following implementation of the arrangements in (a) above, the framework for submission of new policy proposals should include a statement of the intended classification of a proposal against the new classification principles; and
- (d) on a progressive basis, within a timeframe set by Government, agencies should review the classification of their existing programs to ensure conformity with the new classification principles. Finance should issue guidance to agencies on the timetable and processes for this review.

(b) A policy framework for grants administration

There is no whole-of-government policy framework in place for the administration of grants across the Commonwealth. Individual agencies have issued policy guidelines, sometimes in the form of Chief Executive Instructions (CEIs),²² but these guidelines are agency-specific, vary widely in their terms from agency to agency, and do not represent a whole-of-government policy framework in any sense.

The lack of any Commonwealth-wide policy guidance on grants is a major gap in the overall framework for grants administration, especially in view of the significant problems which have arisen in this area over recent years (as evidenced in the ANAO's audit reports). The devolution principle, under which responsibility is devolved to Chief Executives for the management of their agencies, is not inconsistent with a strong framework of central policy guidance; on the contrary, such a framework should help to provide assurance that devolved administrative arrangements give proper effect to Commonwealth-wide requirements for effective and efficient grants administration.

The document that comes closest to a whole-of-government policy statement on grants administration is the ANAO's *Better Practice Guide*, designed to provide practical assistance to officers responsible for the planning, project selection, management and review of grant programs within the Commonwealth.²³ In the absence of any other whole-of-government guidance in the grants domain, this Guide has come to be used, virtually by default, as the *de facto* statement of Commonwealth policy requirements in relation to grants. It has also served as the basis for the ANAO's audits of grant

22 Issued under Section 52 of the FMA Act and FMA Regulation 6. For example, the Finance Chief Executive has issued a CEI on Administration of Grants (CEI 4.8, March 2002).

23 Australian National Audit Office, *Administration of Grants: Better Practice Guide*, May 2002

programs, and is regularly cited in the ANAO's audit reports. The ANAO has indicated its intention to update the Guide to cover more fully some of the issues raised in its recent audits of grant programs, and to reflect changes in the public sector environment more generally.

The *Better Practice Guide* has served an invaluable purpose in promoting the principles of sound grants administration, and continues to be widely consulted and used across Commonwealth agencies. It is not designed, however, as a policy document as such: rather, as a means of assisting agencies to improve their performance and management practices, having regard to legislative and other requirements, the outcomes of relevant performance audits and some general principles of good practice in the administration of grants. Any central framework of policy guidance on the administration of grants should properly be determined and promulgated by the Government itself, from which point the ANAO would conduct its grant program audits against that framework.

The analogy with procurement is relevant here. A whole-of-government framework is in place for procurement, as described in the *Commonwealth Procurement Guidelines* (CPGs).²⁴ The CPGs have legislative authority, being issued by the Finance Minister under FMA Regulation 7. FMA Regulation 8 requires officials performing duties in relation to procurement to have regard to the CPGs, and where an action is taken that is not consistent with the Guidelines, to make a written record of the reasons for that decision.

The CPGs themselves are largely principles-based. They contain some specific obligations and mandatory requirements, reflecting procurement-related obligations arising from other mandatory elements of the financial framework²⁵; however, these are kept to the minimum necessary to meet any essential, whole-of-government requirements, and agencies have substantial scope to apply the Guidelines in a manner suited to their particular circumstances and needs. Further, the ANAO conducts its audits of Commonwealth procurement activity against the framework established by the CPGs, as well as referencing various ANAO procurement-related *Better Practice Guides*.²⁶

The current version of the CPGs took effect from January 2005, and has led to a much clearer understanding of agencies' obligations when they are performing duties in relation to procurement. There is now far greater consistency in the interpretation and application of procurement policy, as well as a higher level of transparency and accountability in the management of procurement processes by individual agencies. Finance played an important role in securing these improvements, in part by developing the CPGs on behalf of government but also by promoting and explaining the new policy framework to agencies. Agencies in turn reformed their own procurement processes to meet the requirements of the CPGs, and invested significantly in the training of their officers. This has contributed to a marked improvement in the professionalism of procurement activity across Commonwealth administration as a whole.

The Review considers that, to support improvements in the quality and professionalism of grants administration across the Commonwealth, similar reforms now need to be put in place in relation to grants. A key first step would be to develop and implement a whole-of-government framework of policy guidance on the administration of grant programs. As in the procurement setting, that framework should be largely principles-based, with prescriptive rules and mandatory requirements

24 Minister for Finance and Administration, *Commonwealth Procurement Guidelines*, January 2005

25 For example, the requirements associated with FMA Regulation 9.

26 See, for example, Australian National Audit Office, *Implementation of the revised Commonwealth Procurement Guidelines* (Audit Report No. 21 of 2006-07).

kept to a minimum. Like the CPGs, the new grants policy framework should have legislative authority via provisions similar to those in the current FMA Regulations 7 and 8, such that officers performing functions in relation to the administration of grants would need to have regard to the terms of the policy framework in carrying out their duties.

The Review considers that there would still be a valuable role to be played by a publication such as the ANAO's *Better Practice Guide*, but as a companion document to the whole-of-government policy framework rather than as a free-standing document in its own right. Accordingly, the Review suggests that the ANAO should work in close consultation with Finance in developing the next edition of the *Guide*, maintaining a focus on practical advice and guidance to grant-administering agencies.

Recommendation 2

The Review recommends that:

- (a) a whole-of-government policy framework be developed for the administration of grant programs across the Commonwealth;*
- (b) the new grants policy framework be principles-based, with prescriptive rules and mandatory requirements kept to a minimum;*
- (c) the new grants policy framework be established under the Financial Management and Accountability Regulations 1997 in the form of guidelines issued by the Finance Minister, with a requirement that Ministers and officials performing functions in relation to the administration of grants should have regard to those guidelines, and comply with any mandatory requirements; and*
- (d) in consultation with Finance, the ANAO should review and re-issue its Better Practice Guide on Administration of Grants to reflect the new policy framework for the administration of grants.*

(c) Financial management framework

The *Financial Management and Accountability Act 1997* (FMA Act) provides the central legal framework for financial management within the Commonwealth. This legislation, along with its supporting FMA Regulations and FMA Orders, sets down the fundamental principles and essential rules to be followed in managing the Commonwealth's resources. Among the matters covered by the FMA Act are specific requirements relating to the care, custody and expenditure of public money;²⁷ the care and disposal of public property; banking arrangements; the maintenance of appropriate financial records; and procurement.

27 'Public money' is defined under section 5 of the FMA Act as money in the custody or under the control of the Commonwealth; or money in the custody or under the control of any person acting for or on behalf of the Commonwealth in respect of the custody or control of the money; including such money that is held on trust for, or otherwise for the benefit of, a person other than the Commonwealth.

Section 44 of the FMA Act places a responsibility on the Chief Executive of each FMA agency to manage the affairs of the agency in a way that promotes the proper use – that is, the efficient, effective and ethical use – of Commonwealth resources.²⁸ Part 4 of the FMA Regulations, *Commitments to spend public money*, sets out a hierarchy of requirements that need to be satisfied, in the appropriate sequence, in order for a commitment to spend public money to be lawfully made. Within that hierarchy, FMA Regulation 9 requires the approver of a proposal to spend public money to ensure, after making such inquiries as are reasonable, that the proposed expenditure is in accordance with the policies of the Commonwealth and will make efficient and effective use of public money.²⁹

Although the FMA legislative framework applies to all proposals and decisions to spend public money, including grants, it makes no specific reference to grants as such. Despite the strength of the financial management framework generally, there has been some significant uncertainty, at least at agency level, about the application of that framework to the administration of grant programs in particular. Key areas of uncertainty highlighted in various ANAO audit reports have included:

- who exactly is exercising approval powers, and their authority for doing so;³⁰
- the point at which an approval of a spending proposal occurs under FMA Regulation 9;
- the application of the financial management framework to Ministers, where Ministers are exercising the role of ‘approver’ under the FMA Regulations;
- the interpretation of ‘reasonable inquiries’ for purposes of FMA Regulation 9;
- the interaction between FMA Regulations 9 and 10, and the sequence in which particular authorisations need to be obtained and processes followed;³¹
- whether high-level policy decisions or in-principle approvals (including any public announcements made by Ministers) constitute an approval under FMA Regulation 9;
- the status of election commitments to spend public money in the form of grants, and requirements attaching to the approval of such commitments following an election;
- requirements for the documentation of decisions relating to the approval of grants;³²

28 Under the *Framework Legislation Amendment Bill 2008*, currently before the Parliament, an amendment is proposed to Section 44 of the FMA Act which would define the ‘proper use’ of Commonwealth resources to mean ‘efficient, effective and ethical use that is not inconsistent with the policies of the Commonwealth’. This amendment is designed to reinforce the long-standing requirement imposed by FMA Regulation 9 that approvers must ensure that a spending proposal is efficient, effective and in accordance with the policies of the Commonwealth.

29 FMA Regulation 9 also requires that, if the proposal is one to spend ‘special public money’, it is consistent with the terms under which the money is held by the Commonwealth. Some limited exceptions to these requirements are prescribed in part (2) of the Regulation.

30 FMA Regulation 3 provides that an ‘approver’ includes a Minister, a Chief Executive or a person authorised by or under an Act to exercise the function of approving proposals to spend public money. FMA Regulation 11 provides that an official must not approve a proposal to spend public money unless authorised by a Minister or Chief Executive, or by or under an Act, to approve the proposal.

31 FMA Regulation 10 prohibits the approval of a spending proposal that is not fully supported by an available appropriation, unless the Finance Minister has given written authorisation for the approval. Where authorisation under FMA Regulation 10 is required, this must be obtained before a spending proposal is approved under FMA Regulation 9; in turn, approval under Regulation 9 is required before a person may enter into a contract, agreement or arrangement under which public money is, or may become, payable.

32 FMA Regulation 12 requires that, if an approval of a proposal to spend public money is not given in writing, the approver must record the terms of the approval in a document as soon as practicable after giving the approval. There is no requirement under the current FMA Regulations to record the *basis*, as distinct from the *terms*, of a Regulation 9 approval. This issue is further discussed in Chapter 3.

- > arrangements for entering into a contract, agreement or arrangement with another party or parties to a grant;³³ and
- > the implications of amending a spending proposal, or varying the terms of a grants contract, agreement or arrangement: in particular, whether such amendments fall within the scope of existing approvals and authorisations, or effectively constitute a new spending proposal (such that a fresh assessment under the FMA Regulations is required).

On many of these issues, the provisions and requirements of the financial management framework are quite clear, at least at the level of principle, to those with an intimate knowledge of the FMA Act and Regulations. The problem, however, is that the same level of knowledge and understanding has often been not held by the officers responsible for the administration of grant programs within particular agencies or even, in some cases, by Ministers responsible for approving the expenditure of public money in the form of grant program funding. The ANAO's performance audit reports have highlighted many cases in which there has been confusion and uncertainty on the part of grant-administering agencies as to how the requirements of the FMA legislative framework apply to the circumstances of their particular grant programs.

For the most part, the FMA Act and Regulations are expressed in the form of broad principles and general requirements – suitably and necessarily so, given that the scope of this legislation covers the entire sphere of Commonwealth administration. The need remains, however, to translate these requirements into more operational terms and to provide some practical and helpful guidance to agencies, having regard to the many problems encountered in the grants domain especially over recent years.

On 20 June 2008 Finance issued Finance Circular 2008/06, *Commitments to spend public money (FMA Regulations 7 to 13)*, designed to assist FMA Act agencies to understand and comply with their obligations when making commitments to spend public money. The Finance Circular is comprehensive in its coverage, and covers all forms of spending proposal; although not focused specifically on the area of grants, it usefully covers a range of issues which have been raised in the ANAO's audits of grant programs in recent years. For example, it includes advice on the role to be played by agencies when advising their Ministers on the exercise of their responsibilities as approvers of spending proposals.³⁴

The new Finance Circular should assist agencies in understanding the requirements of the financial management framework and in applying those requirements in their particular program setting. A factor which adds unnecessary confusion and complexity in these matters, however, is the structure of the FMA Regulations themselves. Part 4 of the Regulations, relating to commitments to spend public money, is unduly complex in its current form, and the sequence of individual Regulations does not align well with the order in which key administrative processes typically occur, or need to occur. An obvious example is the fact that the requirements of Regulation 10 need to be satisfied, where applicable, before a spending proposal can be approved under Regulation 9, whereas the sequence of the regulations would tend to indicate otherwise. There are also other, less obvious, examples.

33 FMA Regulation 13 stipulates that a person must not enter into a contract, agreement or arrangement under which public money is, or may become, payable unless a proposal to spend public money for the proposed contract, agreement or arrangement has been approved under Regulation 9 and, if necessary, in accordance with Regulation 10.

34 In framing their advice and recommendations to a Minister on the approval of grant program spending, agencies as a matter of course should take appropriate steps to advise the Minister whether sufficient authority is in place for the approval, particularly in relation to FMA Regulation 10, and of the Minister's statutory obligations as an "approver" under FMA Regulation 9.

The Review considers that there is scope to shorten and simplify the current set of Regulations in this area with a view to improving their logical sequence, increasing their clarity, and promoting consistency of interpretation and application by agencies.³⁵ While this is not an urgent matter, the Review suggests that the Regulations should be reviewed and restructured at the next reasonable opportunity, with the process to be completed by no later than June 2009. Finance Circular 2008/06 should then be updated and reissued to reflect the new set of Regulations.

Recommendation 3

The Review recommends that:

- (a) at the next reasonable opportunity, and by no later than June 2009, the current FMA Regulations relating to the approval of spending proposals should be reviewed and restructured with a view to improving their logical sequence, increasing clarity, and promoting consistency of interpretation and application across FMA Act agencies; and*
- (b) subject to the implementation of (a) above, Finance Circular 2008/06 should be updated and reissued to reflect the new set of FMA Regulations.*

(d) Information collection and reporting

Another major gap in the current framework for grants administration relates to arrangements for the collection and reporting of information on grants across the Commonwealth. A comprehensive, whole-of-government reporting framework is essential in this area if government is to be well informed in the decisions it makes both on individual grants and on grants policy generally. Effective disclosure and reporting arrangements are also important for reasons of transparency and public accountability: in particular, reliable information on the availability of grants and the details of grants awarded is a precondition for public and parliamentary confidence in the quality and integrity of grants program administration. On neither count are current arrangements satisfactory.

As noted in Chapter 1, Finance is responsible for managing a central database called the Discretionary Grants Central Register (DGCR). Every six months, each Commonwealth agency is required to submit a report to Finance providing details, in a prescribed format, of grants approved under each discretionary grant program for which it is responsible. On the basis of this information, Finance produces a six-monthly report to the Prime Minister, Treasurer and Minister for Finance and an annual report to the Expenditure Review Committee on the overall scale of discretionary grant activity across the Commonwealth and any significant whole-of-government trends. While these arrangements are reasonable as far as they go, they suffer from a number of major limitations.

Implemented in 1998, the DGCR is a cumbersome system, with poor functionality and limited analytical capabilities. It is poorly connected with line agencies' own information systems, and largely for that reason, places a heavy administrative burden on reporting agencies. The coverage of the register is not comprehensive, even in the 'discretionary grants' domain: many categories of grant are exempted

³⁵ For example, the current set of Regulations could be restructured more clearly and simply along the following lines: Spending Proposals (including authority and authorisations); Approval of Spending Proposals; Recording of Approvals; and Entering into Contracts or Agreements. At the same time, the opportunity could be taken to improve the consistency of the Regulations with relevant provisions of the FMA Act. One option to be considered in this regard would be to amend the reference to "efficient and effective", in the current Regulation 9, to "efficient, effective and ethical", consistent with the requirements placed on Chief Executives under Section 44 of the Act.

from reporting requirements³⁶ – in some cases, without any obvious rationale – and there is anecdotal evidence that some agencies choose to ignore their reporting obligations.

The data captured by the DGCR are of highly variable quality, with many inconsistencies both across agencies and over time. Quality assurance processes are not robust. More fundamentally, a major limitation of the DGCR is that its use is confined to government alone, with no provision for public access to the information collected. This contrasts with the reporting system operating in the procurement area,³⁷ which was specifically designed to meet transparency and public accountability objectives.

For all of these limitations, the DGCR is the only source of whole-of-government information on discretionary grants at present, and therefore needs to be retained until better arrangements can be put in place. For the medium term, the Review considers that a new reporting system should be designed and implemented, in close consultation with agencies, with public accountability as well as intra-government use a key design objective. Finance should take responsibility for developing this new system and implementing new reporting arrangements, along with the ongoing collection and reporting of whole-of-government information on the administration of grants. These matters are discussed in more detail in Chapter 4.

Recommendation 4

The Review recommends that Finance retain responsibility for the collection and reporting of whole-of-government information on the administration of grants, and for implementing the new reporting arrangements recommended in Chapter 4.

Investing in a new grants framework

A significant investment of resources will be needed to address the serious framework deficiencies identified in this chapter, and to put in place more robust and effective arrangements for the future. Having regard to the scale of work required, the Review considers that a dedicated unit should be established within the Finance to coordinate the development of a new policy framework for grants administration and to oversee its implementation across the Commonwealth. The new unit should consult closely with line departments and agencies during the development phase of its work; moreover, when a new policy framework for grants has been fully developed and endorsed by government, the unit should actively engage with agencies both to explain the terms of the new framework and to assist them in implementing its requirements. On an ongoing basis, the unit should serve as a 'port of call' and source of expert assistance and advice on any matters relating to the interpretation of the framework or the administration of grant programs more generally.

There will be a cost attached to this investment of resources, especially in the developmental phase, but the Review considers that this cost will be significantly outweighed by the long-term benefits which will accrue from a robust whole-of-government framework for the administration of grants.

36 Exemptions include programs involving grants to educational institutions and medical research organisations; emergency payment programs; payments to overseas aid organisations; grants made under commercial industry development programs; payments made to State and Territory governments; and arrangements involving 'service agreements' between the Commonwealth and service providers.

37 The AusTender system (for further details, see Chapter 4).

The corresponding investment made some years ago in the development of a procurement policy framework provides supporting evidence for this view. By dint of that investment, as noted above, there is now a much clearer understanding of procurement policy requirements across agencies; far greater consistency in the interpretation and application of that policy; a higher level of transparency and accountability in the management of procurement processes; a well-designed reporting system for procurement, closely linked to agencies' own information systems; and more generally, a marked improvement in the professionalism of procurement activity across the Commonwealth as a whole.³⁸

Recommendation 5

The Review recommends that:

- (a) Finance establish an identifiable unit within its structure to take responsibility for developing and implementing the new policy framework for grants administration and for co-ordinating action on government decisions arising from this review;*
- (b) the unit established under (a) above should work collaboratively with portfolios and agencies to explain the terms of the new grants policy framework and to assist them in implementing its requirements; and*
- (c) the Government provide funding for Finance to perform the functions at (a) and (b) above.*

³⁸ A Procurement Division continues to operate within Finance; within that Division, a Procurement Policy Branch has responsibility for procurement policy development, providing advice to the Government on the procurement policy framework and developing supporting guidance for agencies.

03

CHAPTER THREE: PLANNING AND DECISION-MAKING ARRANGEMENTS



This chapter deals with planning and decision-making issues in grants administration, including the roles and responsibilities of Ministers and other decision-makers. It highlights the importance of effective planning and design of grant programs, and proposes a number of significant changes to the current decision-making framework.

Planning and design of grant programs

High-quality planning is critical to the success of any grant program. The key objective of the planning process should be to ensure the program is appropriately structured to achieve its intended outcomes, and will be managed in an efficient and effective manner. Transparency in decision-making and accountability for the use of grant funding should be paramount considerations.

The ANAO's recent audit reports provide numerous examples of grant programs in which agencies' planning processes have been seriously flawed, often in multiple respects. In many of these cases, the major problems encountered at a later stage in program administration could have been averted, or significantly ameliorated, had planning processes been more systematic and thorough at the outset.³⁹

The ANAO's *Better Practice Guide* identifies nine key steps in the effective planning of a grant program, as follows:

- > Establish the need for the program
- > Define operational program objectives
- > Develop a risk management plan
- > Design the program for value for money
- > Design the program for accountability
- > Establish performance measures
- > Select funding strategy
- > Consider taxation issues
- > Produce program guidelines

At one level these may seem to be obvious considerations to which any Commonwealth agency or program manager would have regard. In practice, however, a range of factors – including high levels of staff turnover, inadequate training, a lack of effective documentation, and sometimes unreasonable demands to accelerate program spending – have led to short-cuts or oversights in the execution of these basic steps. Some of the key planning messages arising from recent ANAO performance audit reports are summarised below.

39 Consistent with this, the ANAO has advised that, in the next revision of its *Better Practice Guide* on the administration of grants, it intends to place a much stronger emphasis on the 'front-end' processes of program planning and design.

Authority for expenditure

A fundamental requirement at the planning stage is to establish clearly the authority for expenditure on the grant program, and to ensure consistency of program management processes with the requirements imposed by the terms of the authorising decision or legislation.

Some grant programs are authorised by specific legislation that determines the way in which the program is to operate; in these cases, the responsible entity needs to ensure that all processes are consistent with the terms of the governing legislation. Additionally, and more generally, there needs to be a clear understanding of the obligations imposed by an entity's enabling legislation, either the *Financial Management and Accountability Act 1997* (FMA Act) or the *Commonwealth Authorities and Companies Act 1997* (CAC Act).⁴⁰ In the common case that a grant program is managed by an FMA Act agency, the FMA Act and its subsidiary legislation continue to apply except in the rare event that it cannot operate concurrently with other legislation.

As noted in Chapter 2, there has been some significant uncertainty about the application of the FMA legislative framework to the administration of grant programs, and there is a need for stronger central guidance in this respect.

Roles and responsibilities

Another key function of the planning process is to establish clearly at the outset the roles and responsibilities to be exercised by different parties, especially in relation to the exercise of approval powers. In one recent high-profile case, there was significant confusion and debate as to whether the approval of funding under a grant program was being made by the responsible Minister(s) or by agency officials.⁴¹ The confusion stemmed from a number of sources, including a lack of clear documentation, but many of the problems which subsequently arose could have been avoided or at least limited if these issues had been specifically addressed as part of the planning process.

There are various options to be considered in this regard. For example, Ministers may choose to assume comprehensive decision-making powers in relation to a grant program for which they are responsible; alternatively, they may choose to approve the program guidelines and selection criteria but to authorise officials to take decisions on the award of individual grants in accordance with those guidelines. The latter approach can help to manage the risk, and counter the perception, that decisions on the award of individual grants are made for political reasons rather than on the basis of merit. The appropriate arrangement is likely to vary from case to case, depending on the nature and objectives of the program in question, but the options (and associated implications) should be clearly presented to Ministers as part of the planning process. Clarity from the outset is essential.

40 Based on the information reported in the Discretionary Grants Central Register, only four CAC Act bodies currently manage discretionary grant programs on behalf of the Commonwealth: namely, the Australian Sports Commission, the National Library of Australia, the Australian Institute of Criminology and the Criminology Research Council. For most purposes, references to 'agencies' or 'Commonwealth grant programs' in this report should be taken to include these CAC Act bodies and the grant programs they administer.

41 Australian National Audit Office, *Performance Audit of the Regional Partnerships Programme*, (Audit Report No. 14, 2007–08).

Program design

An important matter for consideration in the design of a new grant program is the method by which applications will be sought, received, assessed and selected. A well-structured competitive process, based upon a comparative assessment of applications against a set of pre-determined selection criteria, is most likely to be robust both in fact and perception. The alternative of using non-competitive 'continuous assessment' methods, under which each funding decision is taken separately from the consideration of other applications, poses significant challenges in ensuring transparent, accountable and cost-effective administration, and in demonstrating that all applicants have been treated equitably. Experience with the former Regional Partnerships Programme underlines the point.⁴²

Program guidelines

A clear set of program guidelines is essential for the efficient, effective and consistent administration of a grant program. In the interests of transparency and equity of access, program guidelines should be not only published but actively publicised to potentially interested parties. Agencies also have a responsibility to ensure that their published program guidelines and documented internal procedures are consistently applied through staff training, appropriate supervision and management oversight, and that any departures from those guidelines and procedures are both well informed and appropriately authorised. Potential applicants and other stakeholders have a right to expect that program funding decisions will be made in a manner, and on a basis, consistent with the published program guidelines and selection documentation.

Selection criteria and processes

Processes for the assessment and approval of grant applications, including details of rating scales and methods and the roles to be played by relevant parties, should be articulated and documented as part of the planning process. The extent to which supporting material (such as letters of support) may be taken into account in the selection of successful applications should be clearly set out both in the program guidelines and in related selection documentation.

Documented procedures, consistent with published program guidelines, provide assurance that consistent standards of administration will be applied. Where key aspects of the decision-making process have not been documented, as in several of the cases recently examined by the ANAO, resulting procedural inconsistencies have meant that it has not been possible to demonstrate that all applicants have received equitable opportunities to access funding.

There is a higher risk to the Commonwealth, and to the achievement of program objectives, where administrative and decision-making processes depart from those set out in the published program guidelines and the complementary departmental procedures. Where the waiver of a particular eligibility criterion is proposed in particular circumstances, it is important that this should be appropriately documented and approved by the responsible decision-maker. The circumstances in which such a waiver may be appropriate should be identified and documented as part of the planning process.

42 Australian National Audit Office, *op. cit.*

Risk assessment and risk management

Effective identification and management of risks is now widely recognised as a critical requirement for sound public administration. In the context of a grant program, risk management focuses on maximising the value for money from grant expenditure by identifying and treating potential risks. The *Better Practice Guide* lists no fewer than 16 risks which commonly arise in the administration of grant programs, along with five broad strategies for managing those risks.⁴³

Risk management is not a static, 'once only' activity; rather, it needs to take place both at the preventative stage, at which risks are treated to prevent their occurrence, and also as part of the ongoing management of the program, where the consequences of any emergent risks are mitigated.⁴⁴ The ANAO's audit reports highlight many cases in which agencies' risk assessment processes have been weak or, even where risks have been accurately identified at the outset, these have not been managed effectively in the subsequent administration of the program.

An important part of the planning process should be to ensure that the officers responsible for managing a grant program possess appropriate levels of skill and expertise, including in matters such as the interpretation and assessment of financial reports (where relevant) and the conduct of viability and risk assessments. Program context will be relevant here; thus the skills and experience needed to identify the risks involved in large-scale commercial projects will be very different from those required in the case of small community-based projects submitted by non-profit organisations.

Grant monitoring

The planning process for a new grant program should aim to put in place effective arrangements for monitoring the progress of projects funded under the program, consistent with the identified level of risk. To assist in this, and to provide confidence that a grant will achieve its intended outcomes, it is important that a clear understanding be struck at the outset as to the purposes for which grant funds may be used, and that this be reflected in the terms of the relevant funding agreement. Effective contract management is also essential.⁴⁵

In many cases examined in the ANAO's performance audits, funding recipients have not been consistently required to provide the information necessary for the administering agency to monitor project progress; at the end of the project, as a result, agencies have found it difficult to make an informed judgement as to whether recipients have satisfied their obligations or delivered the outcomes and value for money expected at the time the proposal was first approved for funding.

Agencies should obtain and analyse project status reports from grant recipients in a timely manner and in accordance with relevant legislation and/or funding agreements. Where project delays occur, agencies need to be proactive in seeking further information which will properly inform assessments as to any action that should be taken to minimise financial, project delivery or reputational risks to the program and the Commonwealth.

43 Australian National Audit Office, *Administration of Grants: Better Practice Guide*, May 2002, pages 12–13.

44 Australian National Audit Office, *op. cit.*, page 13.

45 See Australian National Audit Office and Department of Finance and Administration, *Developing and Managing Contracts: Better Practice Guide*, February 2007

The financial and other information to be supplied by grant recipients should be carefully designed to ensure it will provide the responsible agency with appropriate visibility of actual progress achieved. In the case of large-scale and relatively complex projects, the planning process should consider the merits of implementing a risk-based program of site inspections as one means of managing delivery risks.

Where partner funding is required under the terms of a grant program, it is important that project monitoring arrangements should include oversight of the extent to which nominated partner contributions have actually been provided and applied. Likewise, the financial information to be provided by grant recipients should include details of expenditures incurred to date from all funding sources, and not simply those sourced from Commonwealth grants.⁴⁶

Payment arrangements

Payment arrangements under grant programs should be structured in accordance with the Government's broader cash management policy. A key principle underlying that policy is that payments should be made on an as-needed basis only. This promotes efficient cash management by the Commonwealth, at the whole-of-government level, by maximising available interest earnings. It also manages the risk that funds will be spent for purposes other than those intended, or contrary to the conditions attaching to the provision of funding.

The ANAO's audit reports have highlighted a number of cases in which substantial grant funding has been paid upon the execution of a grant funding agreement, irrespective of project cash flow requirements or the extent to which pre-conditions applying to those payments have been satisfied. The result, predictably, has been an increase in risks and costs to the Commonwealth.⁴⁷ It is fair to note that, in a number of the cases cited, the agencies in question had been placed under considerable pressure to accelerate their program spending and to 'get money out the door'.

The development of a schedule of payments, based on need, should be an integral part of the planning process. The appropriate number and size of payments, and the conditions to which they are tied, will vary according to the nature and objectives of the program in question. In the case of small-scale annual grants to community organisations, a single payment will usually be appropriate; by contrast, in the case of complex, large-scale infrastructure projects, or multi-year grants for ongoing service delivery, payments should usually be made on a staged basis, and only as conditions are satisfied and key milestones met. Advance payments should be made only when there is a net benefit in doing so, and subject to appropriate risk management arrangements.

46 The sequence in which partner contributions are made may also be a relevant consideration. In one of the projects examined by the ANAO in its audit of the Regional Partnerships Programme, the New South Wales State Government had agreed to fund the first \$5.181million of project expenditure. Notwithstanding this, 90 per cent of the approved Commonwealth grant (\$450,000 plus GST) was paid to the grant recipient soon after the funding agreement was signed.

47 See, for example, Australian National Audit Office, *Performance Audit of the Regional Partnerships Programme*, (Audit Report No. 14, 2007–08) and Australian National Audit Office, *Administration of Grants to the Australian Rail Track Corporation* (Audit Report No. 22 of 2007–08).

Taxation treatment

The taxation treatment of grants has been a source of significant uncertainty and confusion in recent years. A major contributor to this confusion has been that taxation issues have often been treated as an after-thought, rather than as an integral part of program planning and design. The result has been a lack of clarity, including in publicity materials and application forms, as to whether grants are being provided on a pre-tax or post-tax basis, or whether they will be subject to GST.⁴⁸

Taxation issues are addressed in more detail in Chapter 8.

Performance measurement

Performance measurement has been an ongoing issue in relation to grant programs, and the ANAO's audit reports highlight numerous examples of weaknesses in this regard.⁴⁹

The starting point for effective performance measurement should be a clear identification of a program's objectives and how these relate to broader government policy objectives. Performance indicators then need to be established, covering not only input measures of program activity (such as the number of projects or services funded) but also outcome measures, both intermediate and final, which are clearly related to the achievement of program objectives. Data will usually need to be collected against the performance indicator framework both for individual projects and the program as a whole.

In order to provide any meaningful analysis of a program's performance in achieving its stated objectives, performance baselines need to be established at both the program and project level. High-quality data are essential for this purpose; reporting arrangements should be designed accordingly, and reflected in the terms of funding agreements.

The volume and detail of data required from grant recipients, and the appropriate level of departmental verification, will vary according to the scale, complexity and risk profile of the program in question. Particularly in the case of more complex grant programs, such as those involving multiple funding partners or distributed funding mechanisms, the ANAO's audits have found that an absence of consistently validated data, a lack of agreement on performance indicators and a failure to capture data on intermediate outcomes have significantly limited both the quality of the reporting process itself and the level of assurance that the program is meeting its objectives.

Issues relating to performance measurement in grant programs, including arrangements for program evaluation, are addressed in more detail in Chapter 6.

The foregoing list of issues, while far from exhaustive, is sufficient to demonstrate the point that high-quality planning is crucial to the ultimate success of a grant program. Consistent with this, and with the extensive evidence gathered by the ANAO in the course of its recent performance audits, the Review considers that much stronger assurance is needed that all key considerations relevant to the planning of an efficient and effective grant program have been fully and systematically addressed.

48 For examples, see Chapter 8 below.

49 For examples, see Chapter 6 below.

Guidelines for new grant programs

In December 2007 the Government took a number of decisions designed to strengthen the management of discretionary grant programs across the Commonwealth. These decisions were subsequently promulgated in the form of a set of Finance Minister's Instructions, issued to agencies.⁵⁰ One of the requirements laid down in these Instructions was that guidelines for any new discretionary grant programs must be considered by the Expenditure Review Committee of Cabinet (ERC).

The Review supports strongly the intended purpose of this requirement – namely, to ensure that agencies' planning processes are thorough and that all key considerations have been addressed in the process of designing a new grant program. It notes, however, that program guidelines are sometimes long and detailed documents, especially in the case of the more complex grant programs, and questions whether this is the most efficient means of providing ERC with the assurance it needs in these respects. In some cases, also, an agency may be reluctant to invest in the development of detailed program guidelines until in-principle approval for the program has been obtained from ERC.

As an alternative to ERC's consideration of detailed program guidelines, the Review considers that the information to be reported as part a new policy proposal should be designed to provide assurance that a robust planning process has been undertaken, and that the proposed grant program is appropriately structured to achieve its intended outcomes. It acknowledges that circumstances will sometimes arise, especially in the course of a Budget process, in which a new policy proposal may need to be developed to very tight deadlines, making it difficult to complete a comprehensive planning process in the time available. In these cases, where the information supporting a new policy proposal is not adequate to provide the required level of planning assurance, the Review suggests that any approval of a new grant program should be made on an in-principle and conditional basis only, on the understanding that no payments would be made under the program until the responsible Minister had provided evidence that a robust planning process had been completed. Where additional assurance was needed in any particular case, it would also be open to ERC to require the submission of draft program guidelines (or other appropriate evidence) before the program was formally implemented and any payments made.

50 2008–09 Budget – Finance Minister's Instructions.

Recommendation 6

The Review recommends that:

- (a) *the framework for the planning of new grant programs should be markedly strengthened, providing greater assurance that each of the following issues has been systematically and fully addressed in program design:*
- > *the strategic intent and intended outcomes of the program;*
 - > *expected benefits and deliverables to the Commonwealth;*
 - > *intended beneficiaries (as a class);*
 - > *program structure and design;*
 - > *the development of program guidelines and related documentation;*
 - > *stakeholder consultations (where relevant);*
 - > *decision-making arrangements;*
 - > *selection criteria and selection processes;*
 - > *program governance arrangements;*
 - > *service delivery arrangements;*
 - > *funding agreement (form and term);*
 - > *payment arrangements;*
 - > *expected taxation treatment (based on consultation with the ATO);*
 - > *key performance indicators (including performance baselines and targets);*
 - > *monitoring, reporting and accountability arrangements;*
 - > *evaluation arrangements; and*
 - > *proposed IT platform;*
- (b) *any new policy proposal for the establishment of a new grant program should address each of the matters in (a) above as far as available information allows;*
- (c) *where the information supporting a new policy proposal is not adequate to provide the required level of planning assurance, any approval of a new grant program should be made on an in-principle basis only; in these cases, no payments should be made under the program until the responsible Minister has provided evidence that a robust planning process has been completed; and*
- (d) *the arrangements proposed at (a) – (c) above should replace the current requirement for ERC consideration of detailed program guidelines for a new grant program. Should additional assurance be needed in any particular case, draft program guidelines (or other suitable evidence) could be made available to ERC on request.*

Decision-making in grant programs

Decision-making in grant programs has been a matter of strong public interest, widespread parliamentary and audit scrutiny, and significant political contention in recent times. The reasons for this lie largely in the 'discretionary' nature of many grant programs, the high levels of flexibility built into many application assessment procedures, and the consequent lack of transparency in Ministerial decision-making processes. In such circumstances, it is often difficult to demonstrate that decisions have been taken on the basis of merit, consistent with transparency and accountability principles, rather than for other reasons, including reasons of political self-interest. Perceptions that political factors have played a part in grant decision-making processes have been heightened by the findings of some recent ANAO performance audits, which have established a strong statistical relationship between the relevant Ministers' influence on grant funding decisions and the electorates to which grant funding has been directed.⁵¹

With a view to strengthening the quality of decision-making in grant programs, and improving public confidence in the process, the Finance Minister's Instructions issued in December 2007 introduced a number of new controls on Ministerial approval of discretionary grants. There were three main elements to the new decision-making rules, which can be summarised as follows:

- > Ministers are not to make decisions on discretionary grants without first receiving departmental advice on the merits of the grant application.
- > If a Minister chooses not to follow departmental advice, the decision to award or reject a grant should be referred for determination by a Ministerial Group, following a written submission from the relevant Minister providing reasons as to why a decision should be made against departmental advice.
- > Ministers who are members of the House of Representatives are not to make decisions in relation to grants in their own electorate, even on the basis of departmental advice; instead, these decisions also are to be taken by the Ministerial Group.

The Finance Minister has noted publicly that these should be considered interim arrangements, pending the outcomes of the current review. Accordingly, the Review has considered the merits of the new decision-making rules, including their likely practical implications and consequences. Its broad conclusion is that, while the objectives underlying the new rules are to be strongly supported, there are likely to be more efficient and effective ways of meeting those objectives. The range of considerations supporting this assessment are summarised below.

Consideration of departmental advice

The Review supports retention of the first requirement above: namely, that Ministers should not make decisions on discretionary grants without first receiving departmental advice on the merits of the grant application. This is a prudent control, designed to ensure that where Ministers elect to assume a decision-making role in relation to the award of grants, they are well-informed of the department's assessment of the merits of grant applications and suitably briefed on any other relevant considerations. Accordingly, the Review proposes that a requirement to this effect should be incorporated into the new policy guidelines to be issued by the Finance Minister, as proposed in Recommendation 2(c).

51 See, for example, Australian National Audit Office, *Distribution of Funding for Community Grant Programmes* (Audit Report No. 39, 2006-07) and *Performance Audit of the Regional Partnerships Programme* (Audit Report No. 14, 2007-08).

A key issue to be covered in departmental advice concerns the application of the financial framework to the decision-making process. As noted in Chapter 2, the financial framework governing commitments to spend public money imposes various obligations on decision-makers, including Ministers, when they are making approvals on the award of discretionary grants. The requirements of FMA Regulations 9 and 10 are of particular importance in this respect; in recognition of this, departmental recommendations and related briefing material on the award of grants should explicitly address the requirements of these Regulations.⁵² More generally, where they see the need, departments should take the opportunity to advise their Ministers of their statutory obligations when taking decisions that involve the expenditure of public money; where a new Minister is likely to assume the role of an FMA Regulation 9 approver, for example, it would be appropriate to arrange a formal briefing on the requirements imposed by the financial framework.

It is important also that administering departments avoid any communication with a Minister or Minister's office that may jeopardise, or appear to prejudice, an objective, merit-based assessment of grant applications. This would generally preclude discussions with Ministers' offices on the merits of individual applications before appraisal processes are completed and formal advice presented to the Minister. Should there be a reason, in exceptional circumstances, for the department to discuss the merits of a proposal with a Minister or Minister's office before the completion of its appraisal processes, it would be prudent for this to occur only with the agreement of a senior member of the department's executive. To protect the probity of the selection process, any such discussions should be appropriately documented.

The Review considers that the requirement for prior consideration of departmental advice should apply to all grant spending proposals, including those made in the context of an election campaign. The statutory obligations applying to the approval of spending proposals deriving from election commitments are no different from those attaching to the approval of any other spending proposal; accordingly, departments should provide their Ministers with advice on options for the funding of election commitments, having regard both to a Minister's statutory obligations and the extent to which the spending proposals satisfy the eligibility or assessment criteria for grant programs which might be used to fund the commitments.

In preparing their advice to Ministers on the funding of election commitments, departments have a responsibility to ensure that Ministers are appropriately informed both as to the nature of the spending proposal and whether it is likely to make efficient and effective use of public money (consistent with the requirements of FMA Regulation 9). For this purpose, documentation will often need to be obtained from project proponents providing evidence of need and details of the proposed expenditure, sufficient to allow Ministers to make an informed judgement in carrying out their statutory responsibilities. It is also important that departments advise their Ministers on any measures necessary to manage risks to the Commonwealth associated with the approval and implementation of election commitments.

The situation may arise that a spending proposal deriving from an election commitment satisfies the requirements of the FMA Regulations but fails to meet the eligibility or assessment criteria for the relevant funding program. For example, where a grant program is structured on a contestable basis, the proposal covered by the election commitment may fail to satisfy one or more of the eligibility criteria specified in the grant program guidelines, or alternatively may fail to make the selection cut when it is assessed on its merits against other competing applications. In such circumstances, should the Minister

52 The whole-of-government guidance document proposed in Recommendation 3 above (Chapter 2) would usefully include some practical advice to agencies in this regard.

wish to proceed with the funding of the election commitment, a suitable funding platform for that purpose would need to be found. The Review recognises that circumstances such as this have arisen in the past, and will doubtless arise again in the future; accordingly, it deals further with this matter in the final section of this chapter (pages 18-19, and Recommendation 11).

Decisions taken at variance with departmental advice

Different conclusions can be drawn, quite legitimately, from any given set of information and evidence, and it should be open to a Minister to reach a decision different from that recommended in a department's or agency's advice. That being said, and in view of the sensitivity likely to attach to such decisions, special care will be needed in these cases in order to demonstrate that the relevant program guidelines and selection criteria have been observed, that all grant applicants have been treated fairly, and that the requirements of the financial framework have been met.

In such circumstances, where a Minister disagrees with an agency's assessment and recommendation on any particular grant application, the Review considers that it would be appropriate for the Minister to clearly over-rule the department and document the basis on which the Minister has reached an alternative view.⁵³ It should no longer be acceptable, as has happened in the past, for a Minister to decline to document reasons in such circumstances;⁵⁴ for a Minister to ask the department to restructure its advice and recommendations to accord with the Minister's views and preferred outcomes; or for a department to 'retro-fit' its documentation or records merely to comply with a Minister's wishes or proposed changes, rather than to execute a Ministerial decision.⁵⁵ Further issues relating to the documentation of grant-related decisions are discussed below.

The Review is not persuaded that the referral of such decisions to a Ministerial Group would lead to an improvement in the quality or efficiency of decision-making on grants. There are several reasons for this view:

- > The Administrative Arrangements Order (AAO) places policy responsibility with each portfolio Minister for a defined range of functions, and it seems appropriate in principle that decisions on the award of discretionary grants should be taken by the responsible Minister (or other approver) in the portfolio (or agency) concerned. If some such decisions were required to be taken by another Minister or by a Ministerial Group, formal authorisation would be required under the FMA Regulations.
- > The FMA Regulations require FMA Regulation 9 approvals to be made by a Minister, a Chief Executive or an authorised person, and do not clearly provide for such decisions to be made collectively. In practice, this would probably mean that a final decision on a matter referred to the Ministerial Group would need to be taken by the Finance Minister, following consultation with other members of the Group and after consideration of their views. Additional administrative processes would need to be put in place to obtain and record the views of each member.⁵⁶

53 A similar requirement should apply where the Minister agrees with the agency's assessment and recommendation, but for reasons different from those cited in the agency's briefing advice.

54 Official Committee Hansard, Senate Standing Committee on Community Affairs, Budget Estimates hearing, 28 May 2007, CA 43-44.

55 See Australian National Audit Office, *Distribution of Funding for Community Grant Programmes* (Audit Report No. 39, 2006-07).

56 It is unlikely that the Ministerial Group would meet in person, at least on a regular basis.

- > Where a decision was referred for determination by the Finance Minister or the Ministerial Group, full responsibility and accountability for that decision would simultaneously transfer. The practical consequence would be that the new decision-maker would need to have a detailed understanding of the relevant program's objectives, guidelines, selection criteria and assessment procedures; would need to be suitably briefed on these matters, either by the agency responsible for the program or by Finance; and would need to understand the possible flow-on consequences of any immediate decision taken for other parts of the program in question. Depending on the number of decisions referred to the Ministerial Group, this process might need to be repeated across more than 200 different discretionary grant programs.
- > Hard data are not available on the number of decisions likely to be referred to the Ministerial Group on the grounds that a portfolio Minister decides not to follow departmental advice. In the case of decisions relating to grants within a Minister's electorate, however, it could be expected on arithmetic grounds alone that hundreds of such decisions would need to be referred to the Ministerial Group within the course of any calendar year.⁵⁷ This raises some significant questions about the workload likely to be involved, especially for the Finance Minister; the administrative costs associated with briefing and servicing of the Ministerial Group; and the efficiency of decision-making processes under these arrangements.

In summary, the Review considers that the referral of decision-making powers to a Ministerial Group, or to the Finance Minister on the Group's behalf, is likely to create a range of unintended and undesirable consequences, notwithstanding the sound objectives which gave rise to the establishment of the Group. In the Review's judgement, the risks associated with the decisions in question will best and most appropriately be managed by those Ministers with formal responsibility and detailed knowledge of the grant programs in question; in its view, also, there are other, more efficient ways to strengthen the quality of decision-making in grant programs, and to improve the level of public confidence in those decisions. These include, in particular:

- > the establishment of a whole-of-government policy framework governing the administration of grants (Recommendation 2);
- > a stronger assurance framework governing the establishment of new grant programs, providing clarity from the outset on roles and responsibilities in relation to decision-making and approval processes (Recommendation 6);
- > a strengthening of requirements in relation to the documentation of the reasons for decisions taken on the award of grants (Recommendations 7 and 9, below); and
- > the development of a new central reporting system for grants, a key objective of which would be to increase the level of transparency and public disclosure of grant decisions (Chapter 4).

⁵⁷ Currently, more than 49,000 discretionary grants are approved in the course of a calendar year, and there are 150 federal electorates across Australia. Most of the portfolio Ministers with substantial grant administration responsibilities are members of the House of Representatives.

Recommendation 7

The Review recommends that:

- (a) decisions on the award of grants should be taken by the Minister or other approver in the portfolio or agency with functional responsibility for the program in question;*
- (b) where Ministers assume the role of an approver under FMA Regulation 9, they should be required to receive and consider agency advice on the merits of grant applications, as assessed against the relevant program guidelines, before taking any decisions on the award of individual grants; this requirement should apply to all grant spending proposals, including proposals designed to satisfy commitments made in the context of an election campaign;*
- (c) the advice and related briefing material provided to Ministers on grant program approvals should explicitly address the requirements of the FMA Regulations, making a clear recommendation as to what the Minister is approving and why the agency is recommending the approval;*
- (d) it should be open to a Minister to reach a decision different from that recommended in an agency's advice; in such circumstances, however, or where the reasons for the Minister's decision are different from those cited in the agency's advice, there should be a requirement on the Minister to record the basis on which he or she is satisfied that a grant spending proposal represents an efficient and effective use of public money, and is in accordance with the relevant policies of the Commonwealth; and*
- (e) public assurance on the integrity of decision-making in grant programs should be provided by means of a new policy framework for the administration of grants; a stronger assurance framework governing the establishment of new grant programs; greater clarity of roles and responsibilities in relation to decision-making and approval processes; stronger requirements in relation to the documentation of the reasons for decisions taken on the award of grants; and stronger disclosure and public reporting requirements.*

Grants awarded within a Minister's electorate

The considerations discussed above in relation to circumstances in which a Minister forms a view at variance with departmental advice apply equally to the case of decisions involving grants within a Minister's electorate, where the Minister in question is a member of the House of Representatives. While accepting that these decisions are likely to be sensitive and subject to considerable scrutiny, the Review does not see a strong case to remove such decisions from the power of the responsible Minister, especially in view of the large number of such cases which could be expected to arise in the normal course of business in any year. Instead, it believes that a strengthening of assurance mechanisms, along the lines proposed in Recommendation 7(e) above, should serve to improve the quality of decision-making in these cases and help restore public confidence in the integrity of grant decisions.

Should additional assurance be needed in this area, either on a transitional or ongoing basis, this could be provided by means of a requirement on Ministers to report periodically to the Finance Minister – perhaps every six months – on any decisions they take involving grants within their own electorate, together with a summary statement of the reasons for those decisions. Alternatively, and perhaps more reasonably, this requirement could be limited to cases in which a decision not only involved the Minister's electorate but was taken at variance with departmental advice. As there would be no formal transfer of decision-making powers under this arrangement, the various drawbacks discussed earlier in this chapter would not come into play.

An additional measure, if considered necessary, would be to include details of the electorate(s) in which grants are awarded as part of the information published under any new grants reporting system.

Recommendation 8

The Review recommends that:

- (a) decisions involving the award of grants within a Minister's electorate should remain within the remit of the responsible Minister or other approver in the portfolio or agency concerned; and*
- (b) should additional assurance be required in these cases, beyond the assurance mechanisms noted in Recommendation 7(e), portfolio Ministers who are members of the House of Representatives could be required to report periodically to the Finance Minister on decisions they take involving grants in their own electorate, together with a summary statement of their reasons for those decisions.*

Documentation of decisions

Given the fundamental importance of the approval process in relation to the expenditure of public funds, and for accountability purposes, it is critical that agencies have a clear understanding and record of Ministerial decisions. In that context, as the ANAO has pointed out, the recording of the reasons for Ministers' decisions to approve or not approve a grant application has been widely recognised as sound administrative practice, including in the views expressed by a number of Parliamentary Committees.⁵⁸

Notwithstanding such views, there is no requirement under the current FMA Regulations for Ministers (or other approvers) to document the reasons for their decisions, as distinct from the terms of those decisions, even in cases where they take a different position from the advice presented or the recommendations made.⁵⁹ While it is open to an agency to invite a Minister to document his or her reasons for a funding decision, and this has sometimes been done, it is equally open to a Minister to decline such a request, and this also has been done, as noted above.⁶⁰

In its recent report on its performance audit of the Regional Partnerships Programme the ANAO recommended that, as part of its responsibilities for developing and maintaining the Commonwealth's financial framework, Finance assess the merits of proposing amendments to the FMA Regulations that would have the effect of requiring approvers to document the basis on which the approver is satisfied that the proposed expenditure:

- > represents efficient and effective use of the public money; and
- > is in accordance with the relevant policies of the Commonwealth.⁶¹

58 See, for example, the Senate Committee Report, Finance and Public Administration References Committee, *Regional Partnerships and Sustainable Regions programs*, October 2005

59 FMA Regulation 12 requires that, if an approval of a proposal to spend public money is not given in writing, the approver must record the terms of the approval in a document as soon as practicable after giving the approval.

60 See footnote 12 above.

61 Australian National Audit Office, *Performance Audit of the Regional Partnerships Programme* (Audit Report No. 14, 2007–08), Recommendation No. 2.

In responding to this recommendation, Finance agreed to assess the ANAO's proposal, while noting the importance of having proper regard to considerations of efficiency and cost-effectiveness. In relation to the existing requirement to record the terms of a spending approval, for example, Finance noted that the appropriate mix and level of documentation would vary according to the nature and risk profile of the spending proposal in question, and that approvers are required to exercise prudent judgement in this respect. In the case of smaller or less significant proposals, a receipt or vendor statement signed by the approver would be appropriate; in contrast, a significant and complex spending proposal would necessarily require a more elaborate mix and level of documentation.

In view of the clear evidence of deficiencies and irregularities in past decision-making on discretionary grants, and given public concerns in this respect, the Review considers that there is a strong case to mandate a new requirement on the approvers of grant program spending under FMA Regulation 9 to document the *basis*, as well as the *terms*, of their approvals. Under this requirement, an approver of a grant spending proposal would be required to document the basis on which the approver was satisfied that the proposed expenditure represented an efficient and effective use of public money, and was in accordance with the relevant policies of the Commonwealth. In most circumstances this could be achieved simply and effectively by the insertion of a standard clause to this effect in the terms of the briefing advice presented to the decision-maker. Where a decision was taken at variance with the briefing advice and recommendation, however, or where the reasons for a decision were different from those cited in the briefing advice, a documented explanation of the reasons supporting the final decision would be required.

A blanket requirement to this effect, covering all forms of spending decision under FMA Regulation 9, would be inappropriate for the reasons cited in the Finance comments above; in particular, that there are some categories of spending proposal where the reasons for the expenditure are largely self-evident, and additional documentary requirements would be both burdensome and unnecessary. In order to quarantine the new requirement to the grants domain, therefore, the Review proposes that the requirement be implemented by means of a specific provision inserted into the terms of the FMA Regulations authorising a new whole-of-government grants policy framework, as proposed in Recommendation 2.

Recommendation 9

*The Review recommends that the FMA Regulations authorising the terms of a new grants policy framework require all approvers of grant spending proposals under FMA Regulation 9 to record in a document the **basis** on which the approver is satisfied that the proposed expenditure represents an efficient and effective use of public money, and is in accordance with the relevant policies of the Commonwealth.*

Approval of multi-year discretionary grant programs

In 1998 the previous Government adopted a policy which required all agencies proposing to operate multi-year discretionary grant programs to seek the prior approval of the Finance Minister, unless they were specifically exempted from doing so. The primary purpose of this measure was to regulate the extent to which agencies could commit future year budget funding. Following the introduction of this requirement, about 400 applications were forwarded to the Finance Minister for approval each year.

In 2006, however, the requirement was eased, such that only those multi-year discretionary grants exceeding 36 months in duration and/or \$2 million in value were subject to approval. As a result of this change, the number of multi-year approval requests fell to 114 in 2006 and 63 in 2007.⁶² The approval requirement has continued in the same form under the present Government.⁶³

The Review has examined the rationale for this requirement and concluded that it serves no useful purpose. For one thing, there is no known instance in which an application for approval has been declined under these arrangements; certainly, no application for approval has been rejected during the past two years, and while records prior to 2006 are not readily available, there is no case known to have been turned down over the previous eight years. Just as important, however, is the fact that the approval process effectively duplicates another process of approval by the Finance Minister, and thereby creates both a significant administrative burden and unnecessary red tape.

Separately from the approval process for multi-year discretionary grants, agencies are required to seek the Finance Minister's approval under FMA Regulation 10 in any case where a spending proposal involves expenditure for which an appropriation of money is not authorised by the provisions of an existing law or a proposed law that is before the Parliament. Like the multi-year approval process, this process also aims to control the extent to which agencies can commit future year budget funding without the authorisation of the Finance Minister. In September 2003 the then Finance Minister delegated, within limits, his FMA Regulation 10 powers to agency Chief Executives, allowing them to authorise certain specific spending proposals where there was insufficient appropriation available. In 2004 and again in 2007 the scope of this delegation was broadened further, providing agency Chief Executives with more autonomy over FMA Regulation 10 authorisations.

Under this framework as it currently operates, agency Chief Executives can authorise, under FMA Regulation 10, most multi-year discretionary grant approvals. Even where they have authority to authorise such an approval under FMA Regulation 10, however, they must still seek the approval of the Finance Minister if the grant in question exceeds the limits applying to the separate multi-year approval process – that is, where the grant is longer than 36 months or greater than \$2 million in value. In other words, two separate approval processes are in place, both directed to essentially the same objective, but different in the details of their requirements (including their monetary limits) and each requiring a distinct process of application and approval. In certain circumstances, as a consequence, two different sets of correspondence and briefing material need to be prepared for the Finance Minister's consideration in relation to the same multi-year discretionary grant.⁶⁴

For the reasons just discussed, the Review considers that the approval process for multi-year discretionary grants should be abolished, and subsumed under the authorisation arrangements applying to FMA Regulation 10. Should specific or additional controls need to be placed on the forward

62 A total of 174 multi-year discretionary grants required approval during 2007; of this number, however, only 63 were submitted for prior approval. The remaining 111 grants (in the Families, Housing, Community Services and Indigenous Affairs and Education, Employment and Workplace Relations portfolios) were awarded without the prior approval of the Finance Minister. In 2008, following clarification of the scope and application of the approval process, the Minister for Families, Housing, Community Services and Indigenous Affairs has submitted a block request to the Finance Minister seeking approval of 1,593 multi-year discretionary grants. Other agencies likewise have submitted an increased number of approval requests in 2008.

63 As confirmed in the Finance Minister's Instructions of December 2007.

64 Under the previous government, at one point, two different Ministers (the Finance Minister and the Special Minister of State) exercised the two sets of approval powers, such that briefing papers on the same discretionary grant proposal needed to be sent to both Ministers for approval.

commitment of funds for expenditure on multi-year discretionary grants, over and above those applying through the FMA Regulation 10 authorisation process, this should be achieved by placing specific limitations on the delegation of the Finance Minister's powers under that Regulation. If need be, also, the terms of that delegation could be varied over time, as has happened in the past.

Recommendation 10

The Review recommends that:

- (a) the requirement on Ministers to seek the Finance Minister's approval for the award of certain multi-year discretionary grants be abolished; and*
- (b) should specific or additional controls need to be placed on the forward commitment of funds for expenditure on multi-year discretionary grants, this be achieved by placing specific limitations on the delegation of the Finance Minister's powers under FMA Regulation 10.*

Provision of grant funding outside regular program guidelines

The situation sometimes arises, especially in grant programs involving a high degree of flexibility and discretion, that a Minister may wish to award a grant to a particular organisation or recipient outside of the regular program guidelines. In the case of a contestable grant program, for example, a Minister may be impressed by the quality of a proposal received outside of the normal selection process and wish to support it, notwithstanding that there is no explicit provision for such an approval within the program guidelines. On some occasions in the past, the responsible department or agency has been encouraged, or placed under pressure, to construct a case for funding the application in question; or alternatively, to 'retro-fit' an approval for the application within its previously completed selection processes and recommendations. Proposals of this nature put the integrity of the selection process at risk, and raise significant issues of transparency and accountability. They can also place pressure on the relationship between a Minister and an agency.⁶⁵

The Review considers that, should a Minister wish to have the flexibility to provide grant funding outside of regular program guidelines and processes, but consistent with program objectives, this intention should be made transparent in the design of a new program and authorised specifically in the terms of Cabinet's approval of a new policy proposal; moreover, any limits on a Minister's powers to exercise this flexibility (for example, limits on the maximum size of any individual grant, or on all such grants in aggregate) should be specified in the terms of the Cabinet's approval. In the case of established programs, Ministers and agencies could be asked to review their existing suite of programs to identify any programs in which a Minister may wish to provide grant funding outside of

65 These issues are not confined to Australia. A recent audit by the United States Government Accountability Office (GAO) highlighted a series of cases in which the US Department of Education had made exceptions to its policies on the award of discretionary grants in order to provide funding to particular applicants. In one case, the Department altered its selection methodology after it had developed and recommended a list of grantees; in another, it rescinded and reversed the order of selected grantees after the peer reviewers had completed their assessments; in another again, four grants were awarded for unsolicited proposals that had not been recommended for funding by any of the three reviewers. The audit report noted that these events had taken place prior to 2003; since that time, the Department had taken steps to reform its processes for awarding grants based on unsolicited proposals, and had generally adhered to its new policies. See United States Government Accountability Office, *Discretionary Grants: Further Tightening of Education's Procedures for Making Awards Could Improve Transparency and Accountability*, Report to the Ranking Minority Member, Education and the Workforce Committee, House of Representatives, February 2006

established program guidelines and processes. The results of this review could be reported for Cabinet's consideration in the context of the 2009–10 Budget.

As in the case of any other grant spending proposal, a Minister responsible for approving a spending proposal under such arrangements would be required to ensure that the expenditure in question represented an efficient and effective use of public money and was in accordance with the policies of the Commonwealth. A documented statement of reasons would also be required, consistent with the arrangements proposed in Recommendation 9 above.

An arrangement broadly along these lines already operates within the overseas aid budget, in the form of a 'Mandated Flexibility' allocation; under this arrangement, contingency funding is reserved within AusAID's budget to meet needs that may arise outside the budget context and which cannot be absorbed within existing budget estimates. The rationale is to provide a capacity to respond quickly and effectively to unforeseen overseas aid requirements without jeopardising the Government's agreed aid priorities.

In the grants domain, any similar use of 'mandated flexibility' funding would need to be consistent with the purposes of the relevant appropriation, the objectives of the program in question and the requirements of any governing legislation. It should also be limited to cases in which there is specific Cabinet authorisation or, in the case of established programs, the prior approval of the Finance Minister. For reasons of transparency, any funding quarantined for 'mandated flexibility' purposes should be identified as such within Portfolio Budget documentation. Such quarantined funding should not be portable across financial years: to the extent that funding reserved for this purpose proves not to be required in practice, any unspent balance could be returned to the broader program appropriation for expenditure in accordance with the standard program guidelines.

Recommendation 11

The Review recommends that:

- (a) should a Minister wish to have the flexibility to provide grant funding outside of regular program guidelines and processes, this intention should be made transparent in the design of a new grant program and authorised specifically in the terms of Cabinet's approval of a new policy proposal;*
- (b) any limits on a Minister's powers to exercise the flexibility under (a) above should be clearly specified in the terms of the Cabinet's approval; and*
- (c) Ministers and agencies should review their existing programs to identify any programs in which Ministers may wish to provide grant funding outside of established program guidelines and processes; the results of this review should be reported for Cabinet's consideration in the context of the 2009–10 Budget.*

04

CHAPTER FOUR: DISCLOSURE AND REPORTING ARRANGEMENTS



This chapter examines disclosure and reporting issues in relation to grants. It finds that current arrangements in this area are generally of poor quality, inefficient and lacking both in coherence and transparency. Accordingly, it recommends some major changes for the future, designed to improve the quality and comprehensiveness of grants reporting; strengthen transparency and disclosure requirements; improve public access to grants information; and increase the efficiency of data collection and reporting processes.

Current reporting systems and arrangements

As noted in Chapter 2, effective disclosure and reporting arrangements on grants are essential for reasons of transparency and public accountability. Reliable and timely information on the availability of grants and the details of grants awarded is a precondition for public and parliamentary confidence in the quality and integrity of grants program administration. In addition, a comprehensive, whole-of-government reporting framework is necessary if government is to be well informed in the decisions it makes both on individual grants and on grants policy generally. On neither count are current arrangements satisfactory.

While there are many different sources of information on Commonwealth grants, there is little coherence in the overall structure of that information, particularly from a public accountability viewpoint: even if it were possible to know of and gain access to all the published information sources – a challenging assignment in its own right – it would be impossible to compile a comprehensive and reliable picture of grant program activity across the Commonwealth. The major sources of information of Commonwealth grant programs (and individual grants awarded, in some cases) are discussed briefly below.

Portfolio Budget Statement

As part of the Australian Government Budget each financial year, all General Government Sector agencies are required to contribute to a Portfolio Budget Statement (PBS), tabled in the Parliament on Budget night. The primary function of the PBS is to provide sufficient information, explanation and justification to enable the Parliament to understand the purpose of each item proposed in the Appropriation Bills.⁶⁶

The PBS discloses key information on the proposed allocation of resources to achieve the Government's desired outcomes, and represents an important means by which the Government remains accountable to the Parliament and, through it, to the Australian public. Information published in the PBS includes details of the agency's resourcing and planned spending at the output and administered item level,⁶⁷ as well as the performance indicators and targets against which performance against planned outcomes will be assessed.

In many cases, detailed information on individual discretionary grant programs does not appear in the PBS documentation as such, but is pooled and reported at a higher level of aggregation.⁶⁸ Performance indicators and targets are likewise often published at a fairly high level of aggregation; moreover, as the ANAO has pointed out in several recent reports, there is often a significant disjunction between the

66 An interpretation provision in the Appropriation Bills requires the PBS to be taken into account when interpreting the items in the Appropriations.

67 From 2009–10 it is intended that this information will be reported at the program level.

68 This applies particularly in the case of small-scale grant programs.

performance information which is planned to be collected, as reported in the PBS, and the information which is subsequently reported in an agency's annual report.⁶⁹

The Portfolio Budget Statements for 2008-09 were significantly redesigned with a view to placing a stronger emphasis on key performance information. Further changes are planned for 2009-10, in particular to increase the visibility of information at the major program level.

Annual Report

Annual reports serve to inform the Parliament (through the responsible Minister), other stakeholders, the media and the general public about the performance of an agency in relation to services provided and outcomes and outputs achieved. Copies of an agency's annual report are required to be presented to both Houses of Parliament by 31 October each year.

Guidelines on the preparation of annual reports are set out in the document *Requirements for Annual Reports for Departments, Executive Agencies and FMA Act Bodies*, issued by the Department of the Prime Minister and Cabinet.⁷⁰ Section 14 (2) of these guidelines states that "Annual reports must also include information on discretionary grants"⁷¹ – a requirement subsequently explained to mean that:

*The annual report must contain a list of discretionary grant programmes administered by the department. A list of grant recipients is required to be available, for example, in an appendix to the report, on request or through the Internet.*⁷²

Agencies have interpreted and responded to this requirement in a variety of ways. An examination of annual reports for 2006-07 shows that some agencies choose to publish a list of the individual discretionary grant programs under which funds were approved during the year;⁷³ others provide a broad description of their programs involving discretionary grants (but with no details of expenditure or individual grants awarded);⁷⁴ others provide details of the 'Output Group' within which discretionary grant programs are located, together with some basic descriptive information on each program;⁷⁵ others again report the total value of discretionary grants awarded during the year, but without any program descriptions or information on individual grants;⁷⁶ and one reports details of its individual grants in aid.⁷⁷

While this situation can be explained, to some extent, by the responsibilities placed on individual agencies in a devolved environment, it does nothing to advance the cause of public accountability or meaningful whole-of-government information. The Review considers that the guidelines currently covering these matters should be reviewed and revised with a view to improving the quality, clarity and consistency of the information published in agencies' annual reports.

69 See, for example, Australian National Audit Office, *Tasmanian Forest Industry Development and Assistance Programs*, Audit Report No. 26, 2007-08

70 Department of the Prime Minister and Cabinet, *Requirements for Annual Reports for Departments, Executive Agencies and FMA Act Bodies*, 18 June 2008. The financial statements contained in annual reports are required to be prepared in accordance with the *Finance Minister's Orders for Financial Reporting*.

71 Department of the Prime Minister and Cabinet, *op. cit.*, page 14

72 *ibid.*, page 25

73 For example, Department of Agriculture, Fisheries and Forestry, *Annual Report, 2006-07*, page 282

74 For example, Attorney-General's Department, *Annual Report, 2006-07*, page 267

75 For example, Department of Families, Community Services and Indigenous Affairs, *Annual Report, 2006-07*, page 345

76 For example, Department of Health and Ageing, *Annual Report, 2006-07*, page 248

77 Department of Finance and Administration, *Annual Report, 2006-07*, Appendix D, page 123

Discretionary Grants Central Register

The Discretionary Grants Central Register (DGCR) was established in 1998 as a central database of information on all discretionary grants awarded across the Commonwealth. The key objectives of the Register were described at the time as being:

- > to ensure that grant administrators and Government as a whole were aware of the extent to which recipients were receiving grants from more than one source; and
- > to improve the administration of, and reporting on, discretionary grants.

At the same time, a decision was taken that the Finance Minister should provide an annual report to the Expenditure Review Committee of Cabinet on the overall scale of discretionary grant activity and any significant whole-of-government trends. Such a report has been produced every year since 1998, with the most recent report (on discretionary grants issued in 2007) being considered by ERC in March this year.

The serious limitations of the current Discretionary Grants Central Register have already been noted in Chapter 2. In brief summary only, these include the following:

- > The DGCR is an extremely cumbersome system, with poor functionality and limited analytical capabilities. It is poorly connected with line agencies' own information systems, and largely for that reason, places a heavy administrative burden on reporting agencies.⁷⁸
- > The coverage of the DGCR is not comprehensive, even in the 'discretionary grants' domain: many categories of grant are exempted from reporting, in some cases without any obvious rationale. Exemptions include, for example, programs involving grants to educational institutions and medical research organisations; emergency payment programs; payments to overseas aid organisations; grants made under commercial industry development programs; payments made to State and Territory governments; and arrangements involving 'service agreements' between the Commonwealth and service providers. There is also anecdotal evidence that some agencies have chosen not to comply with their reporting obligations.
- > The data captured by the DGCR are of highly variable quality, with many inconsistencies both across agencies and over time. Definitions of key terms (even basic terms, such as 'discretionary grant') are not clear in all cases, and neither data entry procedures nor quality assurance processes are robust.
- > The DGCR fails to meet even its own stated objectives. A key design objective, for example, was to control the incidence of 'double-dipping' of grants by organisations which lodged applications for grant funding under different programs or across different agencies for the same or closely related purposes. Finance has advised, however, that there is no known case over the past 10 years in which such 'double-dipping' behaviour has been averted by the use of information on the DGCR. Indeed, most line agencies report that, for a variety of reasons, they do not check the DGCR for possible double-dipping before awarding a grant under their programs.⁷⁹

78 One agency has estimated that it spent some \$34,000 in 2007 on meeting its DGCR reporting requirements, mostly on the employment of temporary staff to enter data manually on to the Register.

79 *Source:* Agency responses to correspondence from the Secretary, Department of Finance and Administration, September 2007. Reasons cited included the operation of internal agency processes and controls designed to limit double-dipping (ignoring, however, the scope for double-dipping across agencies); difficulties in accessing and using the DGCR; poor functionality of the system; and deficiencies in data entry standards (making it difficult to be sure that the same organisation or individual will always be recorded on the system in an identical way).

- Another major limitation of the Register is that its use is confined to government alone, with no provision made for public access to the information collected. This contrasts with the AusTender reporting system used in the procurement area, which was specifically designed to meet transparency and public accountability objectives as well as government information requirements.

Individually and collectively, line agencies have been severely critical of the operation of the DGCR, arguing strongly that the system needs either to be substantially reformed or replaced altogether.⁸⁰ The Review supports this position, and agrees that a new reporting system is urgently needed; at the same time, however, it notes that the Register is the only source of whole-of-government information on discretionary grants at present, and therefore needs to be retained until better arrangements can be put in place. Transitional arrangements, including options for easing the current reporting burden on agencies, are discussed in Chapter 9.

Senate Order 192⁸¹

Senate Order No 192 of 20 June 2001 requires Commonwealth agencies to publish on the Internet, in respect of each calendar year and each financial year, a list of contracts to the value of \$100,000 or more entered into during the previous twelve months.⁸² Supporting details, such as the name of the contractor, the amount of consideration, the subject matter of the contract, the commencement date and the duration of the contract must also be included in the listing; in addition, agencies are required to indicate whether the parties to the contract have agreed to maintain confidentiality of any of the contract's provisions, or whether there are any other requirements of confidentiality, and the reasons for the confidentiality.

All contracts, whether for procurement or other purposes (e.g., grants) are required to be reported under the terms of Senate Order 192, unless exempted on certain defined and limited grounds.⁸³ In most cases, agencies have produced separate lists of their procurement and non-procurement contracts in responding to the order's requirements. The ANAO estimated the total cost of compliance with the order at approximately \$2.4 million for all *Financial Management and Accountability Act 1997* (FMA Act) agencies in 2003–04.⁸⁴

The operation of Senate Order 192 over the four-year period 2003-06 was reviewed by the Senate Standing Committee on Finance and Public Administration, in a report published in February 2007.⁸⁵ The Committee noted that compliance with the order had improved over the five years of its operation; that the use of confidentiality provisions in Commonwealth contracts had generally declined over

80 Source: Agency responses to correspondence from the Secretary, Department of Finance and Administration, September 2007, and agency views as expressed at the workshop held on 15 May 2008 (see Chapter 1).

81 Also known as the 'Murray Motion'. Senator Murray made the case to the Senate in 1999 that 'Accountability can be exacted only where those whose responsibility it is to call government to account are themselves possessed of, or are able to obtain, the information necessary to make considered judgments. Information is the key to accountability' (*Senate Hansard*, 26 August 1999, page 7888).

82 The order took effect from 1 July 2001. It was subsequently amended, in various respects, on 27 September 2001, 18 June and 26 June 2003, and 4 December 2003.

83 Grounds for exemption include considerations relating to public interest immunity, compliance with the *Privacy Act 1988* and other statutory secrecy provisions, and cases in which the Commonwealth has given an undertaking to another party that contract information will not be disclosed.

84 Australian National Audit Office, *Reporting of Expenditure on Consultants*, Audit Report No. 27, 2005–06, page 64

85 Senate Standing Committee on Finance and Public Administration, *Departmental and agency contracts: Second report on the operation of the Senate order for the production of lists of departmental and agency contracts (2003-06)*, February 2007

that period; and that the new AusTender system promised to improve the completeness and accuracy of the information publicly available on government procurement contracts – a promise which has since been substantially delivered. Despite these encouraging developments, however, the Committee considered that it would be premature to revoke the order given that the AusTender system would not report on non-procurement contracts (such as contracts for grants), and that reliance on that system alone would therefore result in a reduction in the transparency and completeness of information on government contracts.⁸⁶

In line with this conclusion, the Committee recommended that Finance, in consultation with the ANAO, relevant parliamentary committees and stakeholders:

“... consider reporting arrangements for non-procurement contracts and explore the development of a reporting mechanism comparable to the new AusTender system for this category of contract, and report to the Committee the outcome of this process within six months of tabling of this report.”⁸⁷

The Review supports the intent of this recommendation, noting the Government’s commitment to improving accountability and transparency arrangements across the entire financial management framework.⁸⁸ A well-designed reporting system for grants should be able to provide all of the information required to be reported under Senate Order 192, and considerably more besides. For example, the information currently reported under the Senate order is limited to details of *contracts* to the value of \$100,000 or more entered into during the previous twelve months; by contrast, the information to be captured under a new grants reporting system should be comprehensive in its coverage of all grants, regardless of the value of the grant or the form of the funding agreement used (for example, whether the agreement takes the form of a contract or a deed).

Agency information and reporting systems

Most Commonwealth agencies publish details of their grant programs on their agency websites, providing summary information on the title, description and broad objectives of each grant program. Many websites also provide access to application guidelines and application forms (including options, in some cases, for online submission of grant applications); information on the opening and closing dates for applications; a list of “Frequently Asked Questions”; links to other relevant websites; a copy of the grant program guidelines; and sometimes a draft contract or funding agreement. In a few cases also agencies have chosen to establish a dedicated website for each of their major grant programs, or categories of program.⁸⁹

Agencies meet the costs involved in providing their IT infrastructure, developing their web pages and administering their websites. Depending on the size of a program and the nature of the selection process, there are also other costs to be borne (such as advertising costs and the costs involved in establishing and managing a national assessment centre). FaHCSIA has estimated the average cost of advertising nationally in urban and rural media, for a medium-sized grant selection process, at about \$80,000.

⁸⁶ *ibid.*, pages 41-42

⁸⁷ *ibid.*, Recommendation 2, page 42

⁸⁸ The Department of Finance and Deregulation is currently coordinating a government response to the Senate Committee’s report. It is anticipated that the response will be finalised and provided to the Senate later in 2008.

⁸⁹ For example, the www.communitywatergrants.gov.au website for the water grant programs administered by the Department of the Environment, Water, Heritage and the Arts.

Some agencies (but not all) choose to publish on their websites the details of individual grants awarded under their programs. Even where this is done, however, the format and detail of such information varies widely from agency to agency, such that it is usually impossible to compare information across agencies or to compile information on a whole-of-government basis. The Review acknowledges that some agency websites are rich sources of information on particular grant programs, and are obviously valuable in that respect; however, they are no substitute for a consistent, whole-of-government approach to the disclosure of information on Commonwealth grant programs and the publication of details of individual grants awarded.

GrantsLINK

Launched in May 2001 and re-launched in July 2006, the GrantsLINK system is administered by the Department of Infrastructure, Transport, Regional Development and Local Government (Infrastructure) and is intended to serve as a 'one-stop-shop' for community access to information on government grants. The GrantsLINK website⁹⁰ contains information on some 250 grant programs administered by Commonwealth, state and local government agencies across a wide range of different portfolios and functional areas. GrantsLINK also provides links to other related information portals such as the Regional Entry Point, a portal providing information on government programs and services available for individuals, businesses and communities in rural, regional and remote Australia.⁹¹

While the GrantsLINK concept is attractive at one level, and Infrastructure has done its best to make the system work, the arrangement suffers from a number of serious limitations. These include:

- > Participation in GrantsLINK is entirely voluntary: for example, some Commonwealth agencies have seen benefits in publicising their programs in this way, and have used the system quite extensively; others, however, have never posted any details of their programs on GrantsLINK. In consequence, the coverage of the system is decidedly patchy – very strong in an area such as regional grant funding, but far from comprehensive across the board.
- > There is no strong consistency in the way that information on different grant programs is reported; wide variations are evident both from program to program and across agencies and jurisdictions.
- > Quality standards also vary widely. Infrastructure is heavily dependent on the quality and accuracy of the information supplied by participating agencies; in practice, however, that has varied significantly both from agency to agency and over time.
- > A major effort and commitment of resources is required to maintain the currency of the information reported on GrantsLINK. Despite Infrastructure's best efforts in that regard, the information reported on the website is clearly outdated in a significant number of cases – usually because reporting agencies have not updated their own information.
- > Most significantly, perhaps, the GrantsLINK system is limited to providing broad, descriptive information on government grant programs, and captures no information on the details of individual grants awarded under those programs (as the system was not designed for this purpose).

90 See <http://www.grantslink.gov.au>. Individuals seeking information on grants are presented with two main search methods: either an option of browsing through the most appropriate of the twelve general grant subjects, or an 'Advanced Search' option involving the entry of a keyword, the name of the department administering the grant and the name of the grant program itself (or alternatively, by browsing all available grants on a State-by-State basis).

91 See <http://www.regionalaustralia.gov.au/Index.aspx>. The Regional Entry Point is also managed by Infrastructure.

While the GrantsLINK system has clearly served some useful purposes, particularly in informing regional communities of the availability of government grants, the Review concludes that the system is neither designed to meet, nor capable of meeting, the broader range of transparency and public accountability objectives outlined at the front of this chapter, and should therefore be dismantled as a whole-of-government reporting system. Whether GrantsLINK should continue to operate as a source of grants-related information for regional communities, or for other defined purposes, should be a matter for Infrastructure and its Minister to determine.

Other grant reporting systems

Brief mention should also be made of the Grants Management System (GMS) used to report to the Council of Australian Governments (COAG) on Indigenous grant program funding initiatives. GMS was developed by the former ATSIC in 1997 and implemented from 1 July 1998 as a replacement for its then grants management system (*Insight*). The system was designed to be a grants management tool which would assist in the management of Indigenous funding projects by helping to assess submissions, make offers, process releases, monitor performance and acquit funds.

As currently structured, the GMS is effectively a centralised database system that supports the assessment, management and reporting of grants. The system has been designed with the needs of recipient organisations in mind: for example, an Indigenous community organisation can lodge a grant application quickly and easily via the Internet, and update its organisational details online. Applications are loaded directly into the system, enabling streamlined assessment processes and facilitating the awarding of grants to recipients.

The GMS is confined to Indigenous funding programs alone, and its focus is more on grants management rather than public accountability or transparency objectives. Even so, the scale and performance of the system is impressive: in the 11 months to May 2008, for example, more than \$705 million was released through GMS under some 3000 different funding agreements covering six different agencies.⁹²

A new whole-of-government reporting system on grants

Having regard to the wide range of considerations discussed in the previous section, the Review concludes that there is no realistic alternative but to commit to the development of a new whole-of-government reporting system which is designed to meet both the Government's own information requirements on grants and also, simultaneously, a range of public information, transparency and accountability objectives. Some key design features of any new reporting system are outlined briefly below.

Consultation with agencies

A fundamental requirement is that the system should be developed in close consultation with line agencies, and be well connected to those agencies' own information systems. This is important partly for the obvious efficiency reasons – for example, to remove the need for manual entry of data to meet whole-of-government reporting requirements – but also for the reason that, unless agencies are closely engaged and well consulted in the development of any new system, both system objectives and subsequent system performance are likely to be at risk.

92 Source: FaHCSIA

Comprehensive coverage

The Review proposes that the new system should be comprehensive in its coverage of Commonwealth grants, covering all grant programs and details of all grants awarded (within a clearly defined scope). Again, this is important for a range of reasons: were large-volume, small-scale grants to be excluded from coverage, for example, it would be impossible to compile a reliable composite picture of the total scale of Commonwealth grants activity.

Transparency and public accountability

Transparency and public accountability must be key objectives of any new reporting system. At a minimum, the system should be designed to provide online public access to reliable and up-to-date information on Commonwealth grant programs (i.e., the availability of grants), forthcoming grant selection processes, and details of individual grants awarded (along with a defined range of characteristic information, such as the overall value of the grant). Where relevant, links should also be provided to more detailed information available on agency websites.

Timeliness of reporting

Timeliness of reporting is critical if the information collected is to be meaningful and useful. The Review has considered various options in this regard; on balance, however, it considers it reasonable that agencies should be required to notify the details of any grant awarded within two weeks of the signing of the contract or other funding agreement for the grant in question. This contrasts with the reporting requirement currently in force, whereby agencies are required to publish details of their individual grants on their website within two days of the announcement of a grant.⁹³

Coverage of reporting requirements

It will be essential that the new reporting system be designed in such a way that it can efficiently and simultaneously meet the full range of whole-of-government reporting requirements relating to grants, including Annual Report requirements, ERC reporting requirements (such as those relating to discretionary grants at present) and Senate Order 192 requirements. As far as possible, also, regard should be paid to any major and foreseeable agency-specific requirements in the design of the new reporting system.

Functionality

As noted earlier in this chapter, the current Discretionary Grants Central Register is an extremely cumbersome system, with poor functionality and limited analytical capabilities. These deficiencies should be rectified in the design of a new reporting system.

93 *2008–09 Budget – Finance Minister’s Instructions*. The Review sees it as appropriate that the signing of a contract or other funding agreement, rather than the announcement of a grant, should be the event to which the reporting requirement is tied, as the parties are not bound until the relevant contract or funding agreement is signed. This nexus would also have the advantage of removing any incentive for agencies or Ministers to delay the announcement of, or not to announce at all, the award of a sensitive or potentially controversial grant (as has happened on several occasions in recent years). The Review acknowledges that there can be a significant time-delay – in some cases several months, or even longer – between the announcement of a grant and the signing of a contract or funding agreement.

Quality standards and procedures

Strong standards of quality control, and robust data entry protocols, will be vital to the quality, validity and ultimately the value of the data collected. Quality considerations should be paramount in the design, development and implementation of the new reporting system. Effective documentation will be critical for this purpose.

Learning from the past

Valuable experience has been gained from the development of the AusTender reporting system in the procurement area, and it would make obvious sense to take account of that experience in designing and developing a new reporting system for grants. Indeed, given the strong similarities in the scope and broad objectives of the two reporting systems, it may well be that the system design and infrastructure used for AusTender could serve as the foundation (with suitable adaptations) for the development of the new grants reporting system. Particularly if this proved possible, there may be value in styling the new grants system AusGrants (or similar), in order to highlight the close relationship between the two reporting systems.

The Review notes that, while the development of a new grants reporting system would inevitably entail some up-front investment costs, significant savings could also be expected to accrue over time. For one thing, there would no longer be any requirement for agencies to bear the costs of expensive and highly inefficient manual data entry (given that the new system would be well connected to agencies' own information systems, allowing for easy transfer and download of data). Over time, moreover, it should be possible to build into the system (or at least provide a capacity to do so) an option for the online submission of grant applications and other efficiency-enhancing features. This could lead to potentially major savings in advertising and related costs: as noted earlier in this chapter, the average cost of a national advertisement for a single medium-sized grant program at present is estimated at about \$80,000.

Recommendation 12

The Review recommends that a new reporting system be developed to meet whole-of-government requirements for information on grants, along with a range of public information, transparency and accountability objectives. The new reporting system should:

- (a) be developed in close consultation with agencies, and well connected to agency information systems;*
- (b) be comprehensive in its coverage, covering all grant programs and details of all grants awarded (within a defined scope);*
- (c) provide online public access to information on Commonwealth grant programs (i.e., the availability of grants), forthcoming grant selection processes, and details of grants awarded (with links to more detailed information on agency websites);*
- (d) require agencies to lodge details of any grant awarded within two weeks of the signing of the funding agreement for the grant in question;*
- (e) be designed to meet the full range of whole-of-government reporting requirements relating to grants, including Annual Report requirements, ERC reporting requirements (on discretionary grants) and Senate Order 192 requirements, as well as agency-specific requirements as far as possible;*
- (f) have a high level of functionality and analytical capability, including a range of tailored reporting tools;*
- (g) be based upon strong data quality standards and data entry protocols, supported by effective quality assurance procedures; and*
- (h) have regard to experience gained with the operation of AusTender reporting system for procurement reporting, and be compatible with the design of that system as far as practicable.*

Assurance issues and arrangements

Both for the Government's own purposes, but also for wider reasons of transparency and public accountability, it will be important to be able to demonstrate that any new reporting system has been structured appropriately, and will be capable of meeting its intended objectives; also, subsequently, that it is operating both efficiently and effectively. Among other benefits, this should lead to both parliamentary and public confidence in the integrity of the new system, and clear the way for much-needed reform of the multiple reporting requirements discussed earlier in this chapter.

To provide assurance in these respects, the Review proposes that the ANAO be invited to conduct an audit of the new grants reporting system outlined above. The Review suggests that the audit be conducted in two stages: the first at the detailed design stage, before full implementation, to provide assurance that the system is structured appropriately, in accordance with its intended objectives; and the second at the post-implementation stage, to provide assurance that the new system is operating efficiently and effectively. The ANAO has indicated its willingness to conduct such an audit at an appropriate time, while noting that any final decision would need to be taken in the context of its overall priorities and available resources.

Recommendation 13

The Review recommends that the Australian National Audit Office be invited to conduct an audit of the new reporting system proposed in Recommendation 12. The audit should be conducted in two stages: the first at the detailed design stage, before full implementation, to provide assurance that the system is structured appropriately, in accordance with its intended objectives; and the second at the post-implementation stage, to provide assurance that the new system is operating efficiently and effectively.

Rationalisation of reporting systems and requirements

Once the audit proposed in Recommendation 13 has been completed, and there is adequate assurance that the new reporting system is operating both effectively and efficiently, the Review considers that prompt action should be taken to decommission and dismantle both the Discretionary Grants Central Register and the GrantsLINK system, at least to the extent that the latter serves as a whole-of-government reporting system on grants.⁹⁴ As discussed earlier in this chapter, neither system currently serves its intended purposes well; moreover, all of the information currently collected and reported on these systems could be fully captured, far more efficiently and effectively, by the new reporting system proposed in Recommendation 12. Transitional issues would need to be managed carefully – for example, to ensure that the historical data stored on the DGCR are suitably archived and available for analysis – but the Review sees no case to maintain either of these current systems once the new reporting system is firmly in place and working well.

For similar reasons, there will be a powerful case to review and rationalise the array of whole-of-government reporting requirements in relation to grants, having regard to the high-quality information which should be made available under the new reporting system. Current reporting requirements are uncoordinated and piecemeal, meeting none of their intended purposes either comprehensively or particularly well; in the case of annual reports, for example, there is little by way of meaningful information, reported on a consistent basis, across the Commonwealth.

Similarly, once the new reporting system has been demonstrated to be working both efficiently and effectively, the Review suggests that the Senate be invited to review the operation of, and continuing need for, Senate Order 192. A partial step has already been taken in this direction, in the area of procurement, by virtue of the Senate's recognition that departments and agencies should be able to meet their reporting obligations under the Order by placing the necessary information on the AusTender system.⁹⁵ It would seem logical that the same principle should also apply in the grants domain, especially as the proposed reporting system for grants will capture all of the information covered by the Senate Order and considerably more besides. Indeed, once well-designed and effective reporting systems are in place in relation to both the grants and procurement activities of government, it would be difficult to see any strong argument to maintain the current Senate Order.

94 As noted above, it would be a matter for Infrastructure and its Minister to determine whether the GrantsLINK system should continue to operate as a source of grants-related information for regional communities, or for other defined purposes.

95 Senate Standing Committee on Finance and Public Administration, *op. cit.*, February 2007

Recommendation 14

The Review recommends that, subject to the findings of the audit report proposed in Recommendation 13, and once there is adequate assurance that the new reporting system is operating efficiently and effectively:

- (a) the Discretionary Grants Central Register be decommissioned and dismantled, noting that the information currently collected for purposes of the Register would be fully captured by the new reporting system;*
- (b) the GrantsLINK managed by Infrastructure be decommissioned as a whole-of-government reporting system on grants;*
- (c) whole-of-government reporting requirements in relation to grants be reviewed and rationalised, having regard to the information made available under the new reporting system; and*
- (d) the Senate be encouraged to review the operation of, and continuing need for, Senate Order 192.*

05

CHAPTER FIVE: FUNDING AGREEMENTS FOR GRANTS



This chapter examines the use of funding agreements in the administration of grant programs. It highlights the need for the conditions attaching to grants to be legally enforceable, as a means of ensuring that public money appropriated for grants is used for its intended purposes. It argues that no single form of funding agreement will be appropriate in all circumstances: rather, that 'proportionality' principles should apply, with funding agreements tailored to reflect the nature of the program in question, the conditions attaching to the grant and the nature and level of risks involved. The chapter outlines the circumstances in which particular forms of funding agreement might be used; proposes a checklist of issues to be considered in the drafting of funding agreements; and argues for the use of plain English as far as possible.

Funding agreements in grant programs

A funding agreement is a document signed by the funding provider and the grant recipient setting out the terms, conditions and arrangements under which a grant is to be provided, received, managed and acquitted. In its common usage, and for purposes of this report, the term *funding agreement* refers to a broad and loosely defined group of arrangements under which grants of government funding are provided to individuals, incorporated entities, or other governments pursuant to public policy objectives.⁹⁶ Used in this broad sense, the term does not imply that a funding agreement has any particular legal status: rather, it is the form and substance of the document which gives a funding agreement its enforceability at law. Funding agreements may take the form of a letter of offer, contract, deed of agreement, or memorandum of understanding (MOU). Letters of offer and MOUs may be contracts if the requisite elements of contract formation are present.

The purpose of funding agreements

An effective funding agreement is critical to promote the efficient, effective and ethical use of Commonwealth resources, as required by the *FMA Act 1997*. To this end, funding agreements for grant programs should contain appropriate controls and accountability mechanisms to ensure that grant funds are spent appropriately, that key conditions are met, and that deliverables will be provided within budget and on time. Funding agreements manage risk and resources, specify responsibilities, and set reporting, acquittal and record-keeping requirements. A well-designed funding agreement will also establish the basis for a constructive and cooperative relationship between the grantor and the recipient, providing clarity of objectives and a shared set of understandings and expectations.

Funding agreements should be negotiated and signed before the start date of a grant, in order to ensure that grant conditions are legally enforceable. Objectives and required deliverables need to be clearly articulated, with links to wider government policy objectives as necessary. It is important also that the statements of objectives, deliverables, performance information and accountability arrangements should clearly align, and be mutually reinforcing.

No payments should be made to a grant recipient until the funding agreement is signed, and subsequent payments should be structured according to need, as discussed in Chapter 3. Start-up payments should be limited to cases in which they are specifically required, and deliver a net benefit to the Commonwealth. In the case of large-scale projects involving high-value grants, funding should be paid progressively as milestones are reached and reports or other deliverables are received;

96 The term is also frequently used in a more limited and technical sense to refer to a particular form of legal agreement, specific to grants.

final payments in these cases should be tied to the submission of final product, to an acceptable level of quality.

The financial information to be provided by grant recipients needs to be carefully designed to ensure that it provides the administering agency with appropriate visibility of actual project progress and the financial contributions made, and expenditure incurred, by all relevant parties to the agreement (and not merely from the Commonwealth's own funding).

Problems arise where these common-sense conventions are not observed. For example, the ANAO's performance audit of the former Regional Partnerships Programme⁹⁷ found that:

*"...the department had...structured Funding Agreements to make payments in advance of the need identified by the recipient in its application for funding..... notwithstanding that Funding Agreement pre-conditions applying to those payments had not been satisfied."*⁹⁸

In addition, payments had been made:

*"...in circumstances where the pre-condition or milestone had not been met. In a number of projects examined by ANAO, the risks had been realised, as reflected by expected co-funding not eventuating."*⁹⁹

Failure of the funding agreement to control the payment of grant funds in line with the pre-condition of the receipt of co-funding put the grant project at risk of not achieving its objectives, and the Commonwealth at risk of not expending monies in an efficient, effective and ethical manner.

The importance of enforceability

In keeping with the responsibilities of Chief Executives under s44 of the *FMA Act 1997*, all grant funding agreements must be enforceable and grant monies must be recoverable, or other remedy available, in the event that a grant recipient is in breach of the conditions of grant. The funding agreement is critical in establishing the rights and obligations of the Commonwealth, the conditions to be met by the grant recipient, the terms on which its provisions are enforceable, and the remedies available in the event of any non-compliance.

The ANAO's audit of Australian Rail Track Corporation (ARTC)¹⁰⁰ found that:

*"...there are no contracts, funding agreements or documented governance arrangements that require the ARTC to use the \$820 million in special grant funding on any particular projects or in any particular timeframe."*¹⁰¹

*"...This means that the grants have been paid on an untied basis rather than in a way that ensures the funds are used for the purposes approved by Ministers..."*¹⁰²

97 Australian National Audit Office, *Performance Audit of the Regional Partnerships Programme*, (Audit Report No. 14, 2007–08)

98 *ibid.*, Volume 1, p. 104

99 *ibid.*, Volume 1, p. 75

100 Australian National Audit Office, *Administration of Grants to the Australian Rail Track Corporation* (Audit Report No. 22 of 2007–08)

101 *ibid.*, p. 18

102 *ibid.*, p. 14

and in relation to \$820 million in rail track funding:

“... *there is no legal obligation imposed on the funding recipients to actually comply...*”¹⁰³

The grant was given as an unconditional gift in order to prevent the payment being viewed as tied to a condition or obligation which might give rise to income tax or GST liabilities. The risk of making grants as an unconditional gift rather than by means of a structured funding agreement, however, is that the monies may be spent in a manner not consistent either with the purpose of the appropriation or the intentions of the decision-maker. To compound matters, funds which are gifted may not be recoverable, even where they are spent on other than their intended purposes.

All funding agreements should be drafted to ensure enforceability at law.¹⁰⁴

Recommendation 15

The Review recommends that:

- (a) funding agreements for grants should be designed to protect the Commonwealth's interests by ensuring that public money is used for its intended purposes; and*
- (b) funding agreements should be structured on the assumption that the conditions attaching to a grant are both obligatory and enforceable, and that funds will be recovered, or other remedies applied, in the event of any breach of those conditions.*

Proportionality

As discussed in Chapter 1, grant programs vary widely in their scale and degree of complexity, from simple grants for small amounts to community or voluntary organisations to large-scale funding for complex projects – for example, major infrastructure projects with elaborate governance structures and multiple funding partners. For this reason, no one form of funding agreement will be appropriate in all circumstances: rather, the principle of ‘proportionality’ should be applied, so that funding agreements are tailored to reflect considerations such as the purpose, value and duration of a grant, the deliverables to be supplied, associated conditions of grant, the level of enforceability required, and the nature and level of the risks involved.

Many community grants involve one-off payments to multiple recipients under the same or very similar conditions.¹⁰⁵ As the amounts involved are often quite small, and the risks associated with non-compliance generally fairly low, legitimate questions may arise as to the cost-effectiveness of pursuing recovery action in the event of a breach or default. Nevertheless, the *principle* of enforceability remains essential in the design of a funding agreement, not least as a signal to the other party; for this reason, the *capacity* to recover small grants should be built into the terms of these agreements.

103 *ibid.*, p. 36

104 The precise mechanisms for achieving this need to be sensitive to a range of considerations, including the limits of the Commonwealth's powers under the Constitution.

105 Other community grants, by contrast, support the ongoing delivery of community services, with funding provided to the same or similar organisations more or less continuously over a period of years (see Chapter 1). Stronger accountability arrangements and risk management strategies will generally be appropriate in these cases, in line with the higher level of risk involved.

Industry funding grants typically involve multiple payments of medium to high value, of higher risk, to several recipients. Recipients are generally incorporated associations or companies, and individual agreements can span multi-year periods. A standard form grant agreement will often be tailored for use with individual recipients, setting out the agreement between the parties, with appropriate controls and accountability mechanisms.

Infrastructure grants are often made to consortiums or joint ventures involving state and local government and industry; these are typically high-value and complex commercial transactions, with elaborate governance structures and relatively high levels of risk. Funding agreements must be individually structured to reflect the role, responsibilities and level of control which each of the parties to the agreement is expected to assume. Clarity is essential in this regard if confusion and buck-passing are not to emerge at a later stage. The funding agreement should also detail clearly the arrangements for monitoring of project progress (including site inspections, where appropriate, as a means of managing risks), the key milestones against which progress will be measured, and the remedies available in the event of any significant delays.

The appropriate use of particular forms of funding agreement (letters of offer, contracts, deeds and MOUs), having regard to the value, level of risk and recipient of a grant, is discussed below.

Plain English

Funding agreements have become increasingly long and complex documents – in some cases, quite unnecessarily so. While a degree of complexity is unavoidable at times, there is little point in burdening a simple grant program with a lengthy funding agreement full of complex terms and legal jargon which the recipient is unlikely to understand, and may not even read. In addition, the more complex the terms of the funding agreement, the greater the burden for agency staff administering the grant. Program managers rarely have legal expertise and if funding agreements are hard to understand, they create additional administrative and legal costs and heighten the risk of agency failure in managing the program. They may also put at risk the relationship between the funding agency and the grant recipient.

The ANAO's recent performance audit of the Tasmanian Forests Development Program found, for example, that:

*“DAFF is not adequately monitoring compliance with the funding deeds and this is compounded by inconsistencies and errors within the deeds. The requirements for milestone reports, final reports and audited statements are outlined in the body and schedules of the deed. However, there are inconsistencies, duplication and unclear due dates between these sections of the deed. The content of the final report is also duplicated, to some extent, by the audited statement.”*¹⁰⁶

The use of plain English in funding agreements is essential to remove unnecessary obscurity and complexity, and will assist both the recipient and the grant-giving agency in understanding and managing their obligations. Legal jargon should be avoided as far as possible.

106 Australian National Audit Office, *Tasmanian Forest Industry Development and Assistance Programs* (Audit Report No. 26, 2007–08), page 29

Checklist of issues to consider in drafting funding agreements

While no one form of funding agreement will be suitable in all circumstances, there are nevertheless some general principles and common elements to be considered in developing virtually any funding agreement. It is useful, therefore, to have a checklist of issues which should be considered in the drafting of funding agreements. An indicative checklist is provided at [Attachment D](#).

Recommendation 16

The Review recommends that:

- (a) the funding agreement used in relation to any particular grant should be based upon considerations of 'proportionality': that is, it should be tailored to reflect factors such as the objectives of the program, the scale and complexity of the grant in question, the context in which the grant is made, the length of funding involved, the desired structure of payments, the conditions attaching to the grant, the nature and level of risks involved, and the desired remedies for non-compliance;*
- (b) without compromising the principles of enforceability and proportionality, funding agreements should be cast in plain English as far as possible, with a minimum of complexity and legal jargon;*
- (c) as part of a new policy framework for the administration of grants, Finance should produce a checklist of issues to be considered in the development of a funding agreement, leaving agencies to make detailed decisions in the context of their particular program circumstances and needs.*

Forms of funding agreement and guidance on appropriate use

As grants are subject to binding conditions, and the Commonwealth is obliged to treat grant funding as potentially recoverable in every case, the legal enforceability of funding agreements is essential. As already noted, funding agreements may take a variety of forms: a letter of offer, contract, deed or MOU. Each of these forms of funding agreement is considered below, along with a discussion of the circumstances in which its use would be appropriate.

Letters of Offer

Consistent with proportionality considerations, a letter of offer will usually be the appropriate form of funding agreement for low-value, low-risk grants such as many small community grants. A letter of offer is simply a letter from the grant-giving agency to the recipient containing all relevant information in relation to the grant, including details of key terms and conditions. The letter should be signed by authorised signatories of both the grant-giving agency and the recipient. A signed copy, accepting the offer and its conditions, should be retained by the recipient, with the signed original returned to the agency.

A letter of offer allows the formal recording of an agreement between an agency and the recipient without placing unwarranted burdens on the recipient (for example, detailed accounting and reporting requirements which are better suited to larger organisations and higher value grants with commensurate levels of risk). A letter of offer is particularly suited to small community projects involving limited funds and low levels of risk, such as the projects supported under the Volunteer Small Equipment Grants program administered by FaHCSIA.

Notwithstanding that the risks may be low, and that the costs of any recovery action would need to be weighed against the likelihood of recovering small amounts, letters of offer should nevertheless be structured to provide for enforceability as required. Consistent with this, a letter of offer should identify, as a minimum:

- > the name and ABN of the recipient (if applicable);
- > the name and ABN of the funding organisation;
- > the name and year of the funding program;
- > the dollar value of the grant;
- > the time period of the grant;
- > expected GST treatment;
- > any terms and conditions, including reporting and record keeping requirements or the necessity of producing receipts on request; and
- > remedies in the event of a breach.

A letter of offer may form a contract between the parties where the elements of contract formation are present.

Contracts

Whether an agreement constitutes a binding contract depends on the presence or absence of certain well-defined legal elements of contract formation in the text of the document.¹⁰⁷ Special problems may arise in the context of government contracting, however, in relation to two of those elements: namely, consideration and intention to create legal relations.

Government, in its commercial activities, is generally subject to the same contract principles as private entities, with a strong presumption that commercial arrangements entered into will attract the usual contractual consequences.¹⁰⁸ A possible exception arises, however, where government uses an agreement to achieve outcomes which are peculiarly governmental and have no equal in normal commercial activity.¹⁰⁹ Grants of public money to further the social and economic purposes of government may fall into this category, and the courts have held in particular cases that contracts for the purpose of giving and administering grants are not contracts at all, but conditional gifts.

The leading Australian case in intention to create legal relations is *Australian Woollen Mills*,¹¹⁰ where the Commonwealth agreed to pay a subsidy to manufacturers who bought Australian wool for local manufacturing.¹¹¹ When the scheme was terminated, the plaintiff claimed it was entitled to outstanding payments due under contract.¹¹² However:

107 The four key elements are offer; acceptance; consideration; and intention to create legal relations.

108 Seddon N 2004, *Government Contracts, Federal, State and Local*, Federation Press, Sydney, 3rd edition, p 83

109 *ibid.*, p 84

110 *Australian Woollen Mills Pty Ltd v Commonwealth* (1954) 92 CLR 424 (HC); (1959) 93 CLR 546 (PC)

111 Seddon, *op cit*, p 86

112 *ibid.*

“The [High] Court concluded that there was no offer by the Commonwealth and that therefore anything done by Australian Woollen Mills in response was not an acceptance. ...The Privy Council, on the other hand...held simply that such a scheme did not result in a contract because there was no intention to create legal relations. The arrangement was not a contractual scheme.”¹¹³

High-value grants for major infrastructure (and similar) projects are unlikely to be construed by the courts as failing for lack of consideration or intention to create legal relations, given the highly commercial nature of the transactions involved and the existence of a detailed commercial contract. Grant arrangements most at risk in this regard are medium-sized grants (between large infrastructure grants, on the one hand, and small community grants, on the other) which involve significant levels of funding and a high level of conditionality, but which are not fully and transparently ‘commercial’ in their structure, design and purpose. One option in these cases is to add a clause to a contract to the effect that:

“It is the intention of the parties that this is a contract.”

Assuming that consideration exists, the addition of such a clause may be sufficient to persuade a court of a genuine intention to create legal relations; it needs to be noted, however, that the clause has yet to be tested in litigation. In doubtful cases, where additional assurance and protection of the Commonwealth’s interests is required, the surer and more robust option is to draft the funding agreement in the form of a deed.

Deeds

A deed is a formal contract under seal¹¹⁴ in which certain formalities are followed, with the result that they can be enforced even if consideration is absent from the agreement. Compliance with the formalities attaching to a deed signifies an intention to create legal relations. A deed may be a bilateral (or multilateral) instrument between two (or more) parties.¹¹⁵

In most states and territories, the major difference between expressing a funding agreement as a deed rather than a contract is that a document must be expressed to be a deed and a deed is executed with two signatures (one by a witness who is not party to the agreement) for each party.¹¹⁶ Deeds may be varied in writing if a clause in the deed makes that provision, and may be transmitted by email.¹¹⁷

The use of deeds varies widely across the Commonwealth. Many agencies use deeds regularly; others rarely, if at all. The Departments of Broadband, Communications and the Digital Economy, Health and Ageing, and Agriculture, Fisheries and Forestry all express their funding agreements for grants in the form of deeds, in particular to remove doubt as to consideration and intention to create legal relations.

113 *ibid.*, p 86. *Australian Woollen Mills* was recently confirmed in *McMurtrie v Aboriginal and Torres Strait Islander Commission*, Supreme Court NSW, James J 20448/99, Friday 17 December 2004. Seddon notes that the same issue has arisen in the UK, citing *Arrowsmith S, Civil Liability and Public Authorities* (1992), Earls Gate Press 50-51...grants on conditions which have been held not to be contracts: *R v Secretary of State for Transport; ex parte Sherriff* (no 2) (unreported, The Independent, 12 January 1988) (government grant to encourage the use of rail)...and *Cato v Minister of Agriculture, Fisheries and Food* [1989] 3 CMLR 513 (grant for the decommissioning of fishing vessel in order to reduce fishing fleet).

114 Formalities deriving from the Middle Ages have been that the document be “signed, sealed, delivered” with the intention that it take effect as a deed. In the Australian context these formalities have been replaced by separate legislation covering deeds in each State and Territory. It is no longer required that deeds be sealed.

115 Carter JW and Harland DJ 2002, *Contract Law in Australia*, Lexis Nexis Butterworths, fourth edition, Australia, [312]

116 For discussion of the law of deeds around Australia, see Starke JG, Seddon NC, Ellinghaus MP, Cheshire and Fifoot, *Law of Contract*, Butterworths, 1992, 6th edition

117 See the *Electronic Transactions Act 1999*.

These departments and other agencies also express their variations to deeds and contracts in the form of deeds, with a view to removing uncertainty about consideration for the variation.

As part of its role in implementing any new policy framework for the administration of grants it would be useful if Finance were to promote awareness of the use of deeds as a legitimate form of funding agreement, and provide guidance as to the circumstances in which the use of deeds may be appropriate. It would also be useful if these issues were to be canvassed in the next edition of the ANAO's *Better Practice Guide: Developing and Managing Contracts*.¹¹⁸

Memoranda of understanding

A memorandum of understanding (MOU) is a document describing a bilateral or multilateral agreement between two or more parties. MOUs can be a useful mechanism to:

- > set out details of the services to be provided and the responsibilities of the parties;
- > set performance indicators or standards for the delivery of specified services;
- > formalise arrangements for the custody of information and materials generated as a result of the services provided; and
- > formalise arrangements and processes to resolve disputes.¹¹⁹

Within the Commonwealth, MOUs are often used between departments and agencies as it is not legally possible for an entity that is part of the Commonwealth to enter into a contract with another party that is not a separate legal entity.¹²⁰ In addition, where grant funding is provided by the Commonwealth to another level of government (such as a State government or a local government authority) to conduct an activity or provide a service, the arrangements will often be set out in an MOU.

Where it is possible to do so, MOUs should be drafted in such a manner that they form contracts and are therefore enforceable at law. Beyond the signing of the MOU itself, however, it is good practice to incorporate the terms and conditions of the MOU into a separate contract or deed with the grant recipient.

118 Australian National Audit Office, *Better Practice Guide: Developing and Managing Contracts*, Canberra, 2007

119 *ibid.*, page 24

120 Based on the common law principle that it is not possible for a legal person to contract with himself or herself.

Recommendation 17

The Review recommends that, consistent with proportionality considerations:

- (a) funding agreements for small-scale, one-off grants should generally take the form of a simple letter of offer (having regard, in the drafting of any such letter, to the elements of contract formation and considerations of enforceability);*
- (b) contracts be used in the case of large-scale or complex grants, such as grants for the funding of major infrastructure projects involving high levels of conditionality and multiple funding partners;*
- (c) deeds be recognised and promoted as a legitimate form of funding agreement, especially in the case of medium-sized grants or in circumstances in which there may be room for doubt as to the enforceability of a contract (for example, due to a lack of consideration or a lack of intention to create legal relations); and*
- (d) in consultation with the ANAO, Finance arrange for guidance to be provided to agencies on the use of deeds as funding agreements, and the circumstances in which the use of deeds may be appropriate.*

06

CHAPTER SIX: PERFORMANCE MEASUREMENT AND ASSESSMENT



This chapter examines performance measurement and assessment issues in relation to grant programs. It highlights some major deficiencies in the quality of performance measurement across the Commonwealth, and raises questions about the likely effectiveness of some grant program spending. For the future, it proposes that agencies should be held responsible for ensuring that the information required for effective performance monitoring and evaluation of a grant program is built into the program design. More broadly, it suggests that the Commonwealth should increase its capacity for high-quality and rigorous evaluation, and promote a culture more conducive to the independent scrutiny of program efficiency and effectiveness.

Performance measurement in grant programs

Performance measurement and assessment have been a major, ongoing issue in the administration of Commonwealth grant programs. The following selection of quotes from six recent ANAO performance audits, all finalised within the last 12 months and covering grant programs managed by six separate Commonwealth departments, highlights both the pervasiveness and the seriousness of the problem:

(1) **Parent School Partnerships Initiative** (DEEWR) ¹²¹

“The department has found it difficult to measure the program’s effectiveness and contribution to the achievement of outcomes. In planning the program, the department did not develop objectives that were distinct and measurable from other objectives of the Indigenous Education Program.” (page 16)

“..... due to the many changes to the Performance Indicators (PIs) in the early implementation of the Strategy there is no national coherence of PIs used across this Strategy. The information collected so far is disjointed and ad-hoc with no possibility of comparing data nationally.” (pages 38–39)

“More focussed program objectives would assist the department to develop performance indicators to address the current difficulty in measuring program outcomes” (page 39)

(2) **Emergency Management Australia** (Attorney-General’s Department) ¹²²

“The alignment of these (grant) activities to strategic directions, and their contribution to overall intended outcomes, is often unclear. There would be benefit in EMA undertaking further work to define its roles and responsibilities, review critically its activities and align these with strategic directions, and develop and report measures to allow a better assessment of the impact of its activities.” (page 14)

(3) **Tasmanian Forest Industry Development and Assistance Programs** (Agriculture, Fisheries and Forestry) ¹²³

“These reports provide limited information on the administration of the programs and do not report on performance against the outcome indicators in the portfolio Budget Statements and departmental project plan” (page 17)

“... DAFF did not report against all outcome indicators for the programs in its 2006-07 Annual Report. As a result, Parliament has not been informed of the achievements (or otherwise) of the programs in meeting their objective. Consideration also needs to be given to the performance data being collected for these indicators and the level of departmental verification required. This is particularly important as DAFF has indicated that it intends evaluating the programs when completed in June 2009.” (page 17)

121 Australian National Audit Office (Audit Report No. 29, 2007–08)

122 Australian National Audit Office, (Audit Report No. 27, 2007–08)

123 Australian National Audit Office (Audit Report No. 26, 2007–08)

(4) **Administering Round the Clock Medicare Grants** (Health and Ageing)¹²⁴

“This single broad measure does not capture other key elements of the objectives of the program, particularly the provision of services to areas of high demand. Measuring and reporting the number of services funded does not inform DoHA, Parliament, or the Australian public, about where, when or how these services are being provided, the quality of the service, the patients being treated, or the workforce providing the services. Nor does the indicator assist DoHA’s program managers to manage the program. Overall, the ANAO considers that DoHA could improve the effectiveness of the performance management framework for RTCM.” (page 40)

“In addition, DoHA has not established a performance baseline for the program or its funding components. As such, it will be difficult for DoHA to measure the extent to which the grant categories are meeting their objectives or the success of the overall program. That is, without knowing the level of service provision at the start of the program, it will be difficult for DoHA to assess the extent to which the program has improved access to after hours services.” (page 40)

(5) **Regional Delivery Model for the Natural Heritage Trust and the National Action Plan for Salinity and Water Quality** (Environment, Water, Heritage and the Arts; Agriculture, Fisheries and Forestry)¹²⁵

“At the present time it is not possible to report meaningfully on the extent to which these outputs contribute to the outcomes sought by government The absence of consistently validated data, the lack of agreement on performance indicators and (the lack of) any intermediate outcomes has significantly limited the quality of the reporting process.” (page 16)

“Overall, the ANAO considers the information reported in the DAFF and NHT Annual Reports has been insufficient to make an informed judgement as to the progress of the programs towards either outcomes or intermediate outcomes. There is little evidence as yet that the programs are adequately achieving the anticipated national outcomes Performance reporting has been an ongoing issue covered by the three previous ANAO audits since 1996–97 and should be a priority for attention in the lead up to NHT3.” (page 16)

(6) **Regional Partnerships Program** (Transport and Regional Services)¹²⁶

“... at no stage have effectiveness targets for the Regional Partnerships Programme been set, or reported against by DOTARS. Instead, the department’s performance reporting in relation to the Programme has involved providing broad statistics on the number of approved grants and amount of approved funding As a result, performance information published by the department in its Annual Reports has not provided the Parliament with a balanced assessment of Programme achievement.” (Volume 1, pages 113–114)

Such criticisms are not limited to discretionary grant programs, but extend also to the performance information supporting grant funding provided in the form of specific purpose payments to the States and Territories. In another recent performance audit report, for example, the ANAO has commented that:

“Current performance information in the National Report on Schooling in Australia casts little light on performance variability across the schooling system in Australia, as well as areas in which performance can improve. Most published performance information takes the form of system-wide aggregates or averages which provide no information on the dispersion of performance or results...”

124 Australian National Audit Office (Audit Report No. 25, 2007–08)

125 Australian National Audit Office (Audit Report No. 21, 2007–08)

126 Australian National Audit Office (Audit Report No. 14, 2007–08)

“No information is currently available publicly (or to the Australian Government) on the performance of the government school system in its own right; on how performance varies within the government (and non-government) school systems; on the margin by which students do not meet the benchmark levels of performance (and how this margin varies across school systems and jurisdictions); or on the proportions of students achieving significantly higher than the benchmark levels of performance. There is scope to enhance current performance requirements to assist policy development and decision-making on educational programs and the allocation of resources, to achieve the agreed national goals of schooling.”¹²⁷

The strong criticisms levelled by the ANAO in these respects are not matters of dispute or contention: in every one of the cases cited above, for example, the responsible department agreed with the ANAO’s recommended action and acknowledged the need to strengthen its performance measurement and performance management framework.¹²⁸ In some cases the recommended action was as basic as:

*“collect and where necessary, validate relevant performance data”;*¹²⁹

*“record, analyse and report this data on an ongoing basis”;*¹³⁰ and

“develop, document and implement an effective performance management framework that includes useful, measurable performance indicators that inform future data collection and analysis, and program evaluation.”¹³¹

Effectiveness of grant program spending

An important consequence of these major deficiencies in performance measurement and assessment is that, in many cases, there is no reliable basis on which to measure the impact, efficiency or effectiveness of a grant program: all too often, the data required to make such judgments are simply not available.

Given its principal focus on ‘framework’ issues, the Review has not attempted any detailed assessment of the performance or effectiveness of individual grant programs. The Review considers, however, that to the limited extent that any judgements can be made on these matters, there is strong circumstantial evidence to suggest that Commonwealth grant program spending in recent years has been at best only partially effective, and often of poor quality. Such evidence includes, for example:

- > the large increase in the number of grant programs overall and in the number of individual grants awarded (in the case of ‘discretionary’ grant programs, from a reported 12,200 grants in 2005 to more than 49,000 grants in 2007, with expenditure over this period more than doubling in real terms);
- > the haste with which many programs have been developed, and resultant deficiencies in the quality of program planning and design;

127 Australian National Audit Office, *Specific Purpose Payments: General Recurrent Grants for Government Schools* (Audit Report No. 45, 2007–08)

128 In some cases the agency concerned drew attention, in its response to the ANAO report, to remedial action it had already put in train on its own account. The Review sees it as problematic, however – and symptomatic of a deeper cultural problem – that basic performance measurement issues were not addressed as part of the initial program planning process.

129 Australian National Audit Office: Audit Report No. 26, 2007–08, page 29

131 *ibid.*

131 Australian National Audit Office: Audit Report No. 25, 2007–08, page 41

- > the lack of clear objectives for some programs (as identified in the ANAO's performance audits), reflecting partly the high number of grant programs overall and the close similarities between different programs in their target groups and stated purposes;
- > the lack of detailed performance information and effective monitoring arrangements (as also identified by the ANAO);
- > the lack of any evaluation planning or evaluation strategy – or even, in some cases, any basic consideration of how outcomes and effectiveness will be measured; and
- > the pressures applied in some cases to “push money out the door”, sometimes well in advance of demonstrated need.

The Review notes that issues of program effectiveness will be addressed, in part, in the second element of this review process, but also (in more detail) as part of the work of the Expenditure Review Taskforce.

Why so poor?

In view of the strong evidence, and widespread agreement, that the quality of performance assessment in many grant programs has been extremely poor, it needs to be asked why this is so.

Perhaps the first point to be made is that the bleak picture painted above is not entirely uniform across the Commonwealth. Especially in recent times, and partly in response to the recommendations made in the ANAO's audit reports, some agencies have made genuine efforts to improve their performance in this regard: both FaHCSIA and Infrastructure, for example, have invested considerable resources over the past two years in developing comprehensive grant management processes and related performance management and reporting systems. Likewise, there are still some agencies in which there is evidence of a serious commitment to systematic performance monitoring and rigorous evaluation: the employment evaluation unit in DEEWR, for example, stands out in this regard. Across the Commonwealth as a whole, however, and especially within many line agencies, there is neither a strong capacity for rigorous evaluation and performance assessment nor a clear commitment in these directions from agency leadership.

There are probably many reasons for this unsatisfactory situation. Deficiencies in planning processes, as discussed in Chapter 3, have certainly played a part: in many cases, for example, program objectives and desired outcomes have not been clearly identified and articulated as part of the initial planning process, making it impossible to establish a suitable baseline for performance measurement or to identify appropriate performance indicators. The haste with which many programs have had to be implemented has exacerbated this problem, increasing markedly the risk that important matters will be overlooked in program design and implementation and that significant problems will emerge at a later stage.

Even more serious, in the Review's judgement, is the decline in commitment to rigorous performance measurement and evaluation across the Commonwealth as a whole, and the accompanying decline in analytical and evaluative capability.¹³² This has not been a sudden or dramatic change – rather, a gradual process of attrition and erosion over many years (dating back, at least, to the mid-1980s). The causes of the problem are complex, and are not discussed in detail here; the symptoms of the decline, however, are evident in many forms:

¹³² This trend has been evident across the entire range of government programs and activities, and is confined to the grants area alone.

- Many program reviews are conducted either perfunctorily – simply because they are required to be done – or for self-serving reasons, with a view to perpetuating the program.¹³³
- Rigorous, relatively independent evaluation, designed to measure the efficiency and effectiveness of a program in meeting its defined objectives, is now the exception rather than the norm.
- Where a hard-edged evaluation report or piece of analysis does emerge, with constructive but critical findings, it will often sit for months pending a decision on its release and the development of a ‘release strategy’. Some such reports are never released, even (or maybe particularly) if they are of high quality.¹³⁴
- The size – and more particularly, the quality – of departmental evaluation units has diminished over time, certainly as a proportion of total departmental resources. Nor has this been compensated by any marked increase in external evaluation activity.
- There is little evidence – least of all, perhaps, in the grants domain – of evidence-based policy formulation and review. For example, relatively few agencies can point to a clear connection between the findings of analytical studies or evaluation reports and the development of policy or program responses.
- Evaluation has been downgraded in the culture of many agencies. Issues of performance measurement and effectiveness do not feature strongly in the messages conveyed by many Chief Executives and other departmental leaders; instead, the message is often conveyed that what really matters is the delivery of program ‘targets’ (such as the filling of program places or the spending of the program budget), rather than the quality of that spending or the achievement of any higher-level objectives.

Of course, these are not matters on which hard data are readily available, and the Review accepts that there is a significant element of judgment in many of the observations just made. To the extent that there is truth in those observations, however, they are important matters for concern and attention.

What needs to be done?

Just as the decline in evaluative capacity has been a long-term and gradual process, so any remedial action will inevitably take many years to have any widespread effect. To be effective, any remedial strategy will need to take action on two broad fronts, as outlined below.

Improvements in planning processes

In the case of grant programs, but also more generally, an essential requirement is to improve the quality of the up-front planning process, along the lines discussed in Chapter 3. The new program assurance process proposed in Recommendation 6 will be critical in this regard, providing greater confidence than currently exists that all key considerations relevant to the design of an efficient and effective grant program have been systematically addressed at the outset.

As part of the new assurance framework, agencies should be held responsible for ensuring that the information required for effective performance monitoring and evaluation of a grant program is built

133 The former reviews of ‘lapsing programs’ were a case in point (as acknowledged by Finance in developing its program of ‘strategic reviews’).

134 In turn, this impacts both on job satisfaction (many high-quality researchers and evaluators have left the Commonwealth in frustration over such matters), and also on the quality of subsequent evaluation reports (given the clear message that critical findings are not welcome, even if warranted by the evidence).

into the program design. This means, among other things, that there should be a clear identification of program objectives and desired outcomes, both intermediate and final; that performance baselines have been established and performance indicators set, both at the program and project level; that arrangements have been made (via the provisions of funding agreements, for example) for the collection and validation of key performance data; and that an appropriate evaluation strategy is designed and put in place, with a clear indication of stages, timelines and responsibilities. Finance also needs to play its part in these matters – for example, by recognising that high-quality evaluation carries a cost, and is a legitimate element in the overall costing of a new policy proposal.¹³⁵

The development of performance measures enabling an informed judgement to be made about the achievement of program outcomes should be an essential part of the initial planning process; equally important, however, is the need for comprehensive reporting against those measures in an agency's annual report. As the ANAO has highlighted, deficiencies both in measurement processes and subsequent reporting have often meant that the Government and the Parliament are not fully informed of the achievement (or otherwise) of a program's objectives.¹³⁶ A clear 'line of sight' is needed between individual performance measures and the higher-level objectives and policy priorities which a program is designed to support.

As part of the Government's *Operation Sunlight* project, Finance is managing an 'Outcomes Review' designed to improve the quality, transparency and consistency of outcomes reporting in Budget documentation and annual reports.¹³⁷ The first stage of this project involves a review (being conducted in consultation with agencies) of the current set of agency outcome statements, including their degree of fit with announced government policy priorities; the objective is to make these statements more specific, targeted and measurable. Once a new structure of outcome statements has been developed, on the basis of this work, it is proposed to map all agency programs (including any administered grants, special appropriations and specific purpose payments) to conform with the new structure. Resulting changes are expected to be reflected in the documentation for the 2009–10 Budget.

The work just described should assist in sharpening the focus on desired objectives and outcomes, albeit at a highly aggregated level, and may thereby improve the basis on which program performance can be measured, monitored and evaluated.

Improvements in evaluation and review

For the reasons discussed above, the Review considers that whole-of-government action is needed to improve the quality and rigour of evaluation activity across the Commonwealth, and to promote a culture more conducive to independent scrutiny of program efficiency and effectiveness. In the grants domain specifically, and beyond the immediate work of the Expenditure Review Taskforce, it proposes that an ongoing program of review and evaluation of grant programs should be put in place, designed to meet three broad objectives:

- to strengthen the base of evidence on which judgements can be made about the appropriateness, effectiveness and efficiency of grant programs;
- to critically appraise the performance of individual programs or related groups of programs; and
- to improve the overall quality of grant program spending across the Commonwealth.

135 Finance has commonly expected agencies to 'absorb' the costs of their evaluation activity.

136 Australian National Audit Office, *AUDITFocus* newsletter, April 2008

138 The 2008–09 Budget involved a number of initial reforms, including changes to Budget Paper No. 4 and some redesign of Portfolio Budget Statements.

As a matter of good practice, agencies should plan on the basis that any ongoing grant program should be subject to a formal process of review at least once every five years. Among other purposes, this review would be designed to ensure that the program remained consistent with broader government policy goals, and was meeting its own specific objectives in an efficient and effective manner. Agencies would brief their portfolio Ministers on the results of these reviews, making recommendations for program changes where they saw the need.

Beyond such internally commissioned reviews, and in the interests of rigour and transparency, the Review sees it as important that provision also be made for some major reviews and evaluations of grant programs to be undertaken independently of the agency responsible for the programs in question. This is not to imply that line agencies would not be consulted or engaged in the evaluation process – inevitably they would be, and should be; rather, it acknowledges the fact that objectivity is an important requirement in effective evaluation and that, all else equal, there will be a higher degree of confidence in the findings of an evaluation study conducted at arms length from the agency responsible for administering a program. Indeed, this consideration was an important factor in the development and establishment of Finance’s current program of ‘strategic reviews’.¹³⁸

Recommendation 18

The Review recommends that:

- (a) as part of the planning process for a new grant program, agencies should be held responsible for ensuring that the information required for effective performance monitoring and evaluation is built into program design: in particular, that there is a clear identification of program objectives and desired outcomes, both intermediate and final; that performance baselines are established, and performance indicators set, both at the program and project level; that key performance data are collected and validated; and that an appropriate evaluation strategy is designed and put in place, with a clear indication of stages, timelines and responsibilities;*
- (b) beyond the immediate work of the Expenditure Review Taskforce, an ongoing program of review and evaluation of grant programs be put in place. This program should be designed to strengthen the base of evidence on which judgements can be made about the effectiveness and efficiency of grant programs; critically appraise the performance of individual programs or related groups of programs; and improve the overall quality of grant program spending across the Commonwealth;*
- (c) in the interests of rigour and transparency, some of the major reviews and evaluations to be conducted under the program at (b) above should be undertaken independently of the agency responsible for administering the grant program or programs in question; and*
- (d) more broadly, the Government consider measures designed to improve the quality and rigour of evaluation activity across the Commonwealth; to increase the capacity for high-quality and independent evaluation; and to promote a culture more conducive to independent scrutiny of program efficiency and effectiveness.*

¹³⁸ Finance’s program of strategic reviews is one of the options for conducting independent, arms-length studies of the type described. Other options which might be considered are the establishment of an independent unit responsible for program evaluation and review (broadly along the lines of the Office of Evaluation and Audit, responsible within Finance for the evaluation of Indigenous programs), or the commissioning of particular evaluation studies from external parties (such as universities or specialist research centres). There are pros and cons attaching to each of these options, and judgements may best be made on a case-by-case basis.

07

CHAPTER SEVEN: ACCOUNTING TREATMENT OF GRANTS



The Review's terms of reference require a consideration of issues relating to the accounting treatment of grants, including 'problems in the application of the accounting treatment for different categories of grant under both the Australian Accounting Standards and the Government Finance Statistics, and how compliance can be improved'.

There is no Australian Accounting Standard which deals specifically with accounting for grants payable. AASB 1004, *Contributions*, deals with non-exchange revenue transactions¹³⁹ (including grants), but its focus is predominantly on accounting by the recipient rather than the provider of funds. The provisions of AASB 1004 are derived from AAS 29, *Financial Reporting by Government Departments*, and AAS 31, *Financial Reporting by Governments*; these two standards were withdrawn in December 2007, and their provisions relating to grant accounting transferred to AASB 1004. AASB 120, *Accounting for Government Grants and Disclosure of Government Assistance*, is also broadly relevant, although its focus is on grants received by for-profit organisations.

ISSUES

Adequacy of guidance to grantors

The current accounting standards framework focuses principally on accounting from a grantee's perspective, and provides little by way of definitive guidance to grantors. Neither the accounting standards themselves nor the Generally Accepted Accounting Principles (GAAP) framework¹⁴⁰ make clear in any detail how a grantor, in this case the Australian Government, should account for grants. This uncertainty has led to a variety of interpretations by different Commonwealth agencies on some key accounting issues, such as when recognition of a grant expense should occur and the appropriate accounting treatment of multi-year grants and prepayments.

The key considerations in accounting for grants, from a grantor's perspective, include determination of the point at which control is passed and the establishment of a binding and present obligation. These considerations are relevant, in principle, to all forms of grant, but they are especially important in the case of large-scale, multi-year grant programs such as specific purpose payments to the States and Territories¹⁴¹ and other grant payments made under Commonwealth-State funding agreements. The following example serves to highlight the lack of clarity in these respects, and the scope for differing interpretations of the accounting standards.

Accounting treatment of Commonwealth grants to the States

Prior to 2003 the Commonwealth recognised its grant payments as an *expense* at the point that they were due to be paid to the States, and the States in turn accounted for grant monies when they were due to be received (a due and payable approach). Grant *liabilities* were recognised to the extent that the services required to be performed by the grantee had been performed, or the relevant eligibility criteria had been satisfied. A *commitment* was recorded when the Commonwealth had a binding agreement to make the grants but services had not been performed or criteria satisfied. Where grant monies were paid in advance of performance or the satisfaction of criteria, a *prepayment* was recognised.

139 Transactions (such as grants) involving transfer payments by a government in which the government does not receive approximately equal economic value directly in return.

140 The Generally Accepted Accounting Principles (GAAP) is the standard framework of guidelines for accounting practice, involving a set of standards, conventions and rules to be applied in recording and summarising transactions and in preparing financial statements. GAAP accommodates variations in accounting practices provided that the methods used accord with its general framework of principles.

141 Hereafter abbreviated to 'the States'.

These arrangements were consistent with the underlying principles of accrual accounting: in particular, the principle that recognition of funding should not occur until control had been passed. In July 2003, however, the Commonwealth altered the accounting treatment of its education grants such that an expense was recognised and a corresponding liability recorded at the point that the relevant Ministerial determination was signed (usually at the beginning of each calendar year), rather than when the grant funds were actually paid to the States. This treatment resulted in a variety of anomalies and inconsistencies:

- Grants payable under different Commonwealth-State funding agreements were accounted for in different ways, despite strong similarities in their basic structure and design. Between 2003 and 2006, for example, grants payable under the Commonwealth's health care and education agreements with the States were accorded quite different accounting treatments, notwithstanding that both sets of agreements shared a wide range of common characteristics.
- As grantees, State Governments did not follow the Commonwealth's new accounting treatment of education grants, instead maintaining the due and payable approach. The result was a significant timing difference between corresponding entries in State and Commonwealth accounts.
- Under the Government Finance Statistics (GFS) framework, the Australian Bureau of Statistics (ABS) records education grants when the cash is paid by the Commonwealth and received by the States. The rationale underlying this treatment is that considerations of economic substance, rather than any legal obligation, should determine the passing of control from one party to another, and that no economic benefit is created or transferred by reason of the signing of a Ministerial determination. Following the change made in July 2003, therefore, a significant divergence emerged between the treatment of education grants in the Commonwealth's financial statements under GAAP and the treatment of those grants under the GFS framework – at odds with the objective of harmonising accounting treatments between the two frameworks.¹⁴²
- The financial statements incorporating the different accounting treatments of health and education grants were both audited by the ANAO without qualification, suggesting that the two different interpretations of the accounting standards were both seen as acceptable.

In response to concerns arising in these respects, and to ensure that grant programs to the States were accounted for appropriately and consistently, a review was established in 2007 to examine the grant accounting practices of the Australian Government, the States and Territories and relevant Commonwealth agencies.¹⁴³ In relation to education grants specifically, the review concluded that grants paid to and through the States and other education providers (such as universities) should be recognised on a due and payable basis – that is, when control for a grant passes, with grant conditions being met by the relevant grantee. It noted that an application of this principle should serve to promote consistency of accounting treatments across different Commonwealth agencies, between the Commonwealth as grantor and the States as grantees, and between the GAAP and GFS frameworks.

In line with this approach, the accounting treatment of Commonwealth education grants was changed in the Mid-Year Economic and Fiscal Outlook (MYEFO) estimates update for 2007–08, with the new treatment confirmed in the Consolidated Financial Statements released in December 2007.

142 AASB 1049, released in November 2007, requires governments preparing General Government Sector and Whole-of-Government financial reports to adopt the GAAP treatment that best aligns with GFS. Any divergences from GFS are required to be disclosed in the notes to the financial statements.

143 The review was conducted by a working group comprising representatives of Finance, Treasury, the Australian Bureau of Statistics and the Australian National Audit Office. A draft report prepared by the working group was made available to the Review; however, the report has not been finalised, nor final recommendations agreed.

Review of the accounting standards framework for grants

While the issues highlighted by this example have now been satisfactorily resolved, the fact remains that the current accounting standards framework is ambiguous in some significant respects, and is particularly deficient in the quality of the guidance it offers to grantors. Existing standards admit of a variety of different interpretations and accounting treatments on the part of grantors – a fact confirmed by the results of recent financial statement audits – and as long as this situation prevails, the objectives of consistency, comparability and transparency will all be at risk. Clearer standards and better guidance are needed to support higher standards of consistency and transparency in the accounting practices of grantors.

The Australian Accounting Standards Board has recognised the limitations of existing accounting standards in the area of grants, and has been working in conjunction with the Financial Reporting Standards Board of New Zealand to develop a joint standard which would offer clearer and better guidance to grantors. Progress has been slow,¹⁴⁴ however, and while the Commonwealth is not in a position to dictate the terms of any new standards, it would be appropriate to press the AASB to expedite its consideration of these matters and to ensure that accounting by grantors is dealt with as well as accounting by grant recipients. The Commonwealth's membership of the Financial Reporting Council may provide an avenue of influence in this regard.¹⁴⁵

In the meantime, pending the development of any new accounting standards, the Review considers that Finance should develop and promulgate whole-of-government guidance, not inconsistent with the current accounting standards, on the accounting treatment of grants paid by the Commonwealth. As far as possible, the terms of this guidance should align with the ABS's treatment of grants under the GFS framework and with the terms of any new policy framework for the administration of grants. The objective should be to improve clarity and consistency in the accounting treatment of grants across the Commonwealth, and thereby improve both transparency and accountability. The Review notes that Finance has commenced developing whole-of-government guidance on this issue.

Recommendation 19

The Review recommends that:

- (a) *through mechanisms such as the Financial Reporting Council, the Heads of Treasuries Accounting and Reporting Advisory Committee and direct representation, the Commonwealth should encourage the Australian Accounting Standards Board to expedite its review of the relevant Australian accounting standards with a view to clarifying the accounting treatment of grants, especially from the grantor's perspective;*
- (b) *pending the development of any new accounting standards, Finance should develop whole-of-government guidance, not inconsistent with the current accounting standards, on the accounting treatment of grants paid by the Commonwealth. As far as possible, the terms of this guidance should align with the ABS's treatment of grants under the GFS framework and with the terms of any new policy framework for the administration of grants. Once finalised, this guidance should be promulgated in an authoritative form, such as a Finance Minister's Order.*

¹⁴⁴ The issue was first raised at the July 2005 meeting of the AASB.

¹⁴⁵ The Financial Reporting Council is responsible, *inter alia*, for providing broad oversight of the process for setting accounting and auditing standards. Members of the Council are appointed by the Treasurer under section 235A of the *Australian Securities and Investments Commission Act 2001* and include several public sector representatives.

08

CHAPTER EIGHT: TAXATION TREATMENT OF GRANTS



The Review's terms of reference require a consideration of the basis for determining the taxation treatment of grants. Like many other matters within the scope of the Review, this has been an area of some significant confusion and uncertainty, due partly to the fact that taxation issues have often been treated as an after-thought rather than as an integral part of program design. To assist in its consideration of taxation issues, the Review consulted with Treasury in its role of principal adviser to the Government on taxation policy. Treasury in turn sought the views and advice of the Australian Taxation Office (ATO).

The payment of a grant by a government agency does not have a fixed or 'standard' tax treatment. The tax treatment applicable to any particular grant will depend upon a combination of factors, including the nature and characteristics of the grant (in particular, the purpose of the grant and how the grant funding will be delivered), the status and circumstances of the grantee, and the provisions of any governing legislation. Key considerations, based upon taxation law and relevant taxation rulings,¹⁴⁶ are summarised briefly below.

Taxation of grants to individuals not carrying on a business

In the case of an individual who is not carrying on a business, the receipt of a grant may result in an amount being included in the person's assessable income in any of the following circumstances:

- where the grant has the character of 'ordinary income'.¹⁴⁷ Factors that may indicate that a grant is 'ordinary income' include the following:
 - the grant is a product or incident of any employment or services rendered by the individual;
 - the purpose of the grant is to supplement income or replace income; and
 - the grant is regular, expected and able to be relied upon by the individual to meet living expenses, and is paid to the individual for that purpose;
- where the grant is an employment termination payment;¹⁴⁸
- where the grant is in respect of, or for or in relation to any employment or services provided by the recipient, despite not having the character of ordinary income;¹⁴⁹
- where the grant is received for the disposal, loss or destruction of a depreciating asset used for producing assessable income;¹⁵⁰
- where the grant is received as a recoupment of certain deductible losses or outgoings;¹⁵¹ and
- where a capital gains tax event (CGT event) happens because the grant is received, and there is a capital gain.¹⁵²

146 See, for example, Taxation Ruling TR2006/3, which applies to recipients of government payments to industry designed to assist the recipients to continue, commence or cease business.

147 Such a grant is assessable under section 6-5 of the *Income Tax Assessment Act 1997* (ITAA 1997).

148 The taxable component of an employment termination payment is included in assessable income under Division 82 of the *ITAA 1997*.

149 See section 15-2 of the *ITAA 1997*.

150 See Division 40 of the *ITAA 1997*.

151 See Subdivision 20-A of the *ITAA 1997*.

152 The capital gain may be reduced or disregarded in some circumstances.

The post-tax value of the grant will vary according to the characteristics and circumstances of the individual – for example, the individual's other sources of income and marginal tax rate. By increasing a grant recipient's assessable income, the receipt of a grant may also reduce an individual's eligibility for other government assistance, such as Family Tax Benefit.

Taxation of grants to entities (including individuals) carrying on a business

The receipt of a grant by a business entity may result in an amount being included in the entity's assessable income in any of the following circumstances:

- > where the grant has the character of 'ordinary income'.¹⁵³ Factors that may indicate that a grant is 'ordinary income' include the following:
 - the grant is a product or incident of any services rendered or business carried on by the entity;
 - the purpose of the grant is to supplement income or replace lost income or profits; and
 - the periodicity, recurrence or regularity of the grant;
- > where the grant is received in relation to carrying on a business;¹⁵⁴
- > where the grant is received for the disposal, loss or destruction of a depreciating asset;¹⁵⁵
- > where the grant is received as a recoupment of certain deductible losses or outgoings, and is not otherwise assessable;¹⁵⁶ and
- > where a CGT event happens because the grant is received, and there is a capital gain.¹⁵⁷

Additionally, where a grant is used to cover business-related expenditure, the expenditure is usually deductible against either the grant or other business income. If a grant is used to purchase, or reimburse the purchase of, a depreciating asset, depreciation deductions are generally available over the effective life of the asset.

There are some rare cases in which grants have been specifically exempted from tax by virtue of a government policy decision, subsequently enshrined in legislation. Examples are the grants made available to support restructuring of the dairy and sugar industries, and certain grants for disaster relief. However, other grants provided in similar situations have remained fully assessable. In some cases, grants have been grossed up to offset the tax liability which the grant will attract.

When is a grant included in assessable income?

In most cases, a grant is included in assessable income in the year in which it is received by the recipient or dealt with on behalf of the recipient. In some circumstances – for example, where a grant is made on a conditional basis – a grant is not derived as income when it is received, but as it is earned. If this amount is earned over more than one financial year, an amount may be included over more than one income year. Likewise, an amount of assessable recoupment may be included over more than one income year.

153 Such a grant is assessable under section 6-5 of *ITAA 1997*.

154 Such a grant is assessable under section 15-10 of *ITAA 1997*.

155 An amount equal to the grant may be included in the termination value of the depreciating asset. Where the termination value exceeds the value of the depreciating asset, the excess will be included in assessable income under Division 40 of the *ITAA 1997*.

156 See Subdivision 20-A of the *ITAA 1997*.

157 See footnote 7 above.

Goods and services tax

A grantee will be required to remit 1/11th of a grant payment to the Australian Taxation Office (ATO) as goods and services tax (GST) where the grant satisfies all of the following tests:¹⁵⁸

- the grant represents consideration for a supply;
- the supply is made in the course of furtherance of an enterprise that is carried on by a supplier;
- the supply for which the grant is consideration is connected with Australia;
- the entity making the supply (the grantee) is registered, or required to be registered, for GST; and
- the supply is not GST-free or input-taxed.

The central question is whether a grant is consideration for a supply made by the grantee. The concept of supply is very broad. It includes the supply of goods and services, the provision of information, the creation, grant, transfer, assignment and surrender of rights, and the entry into, or release from, an obligation.¹⁵⁹

There are no provisions in the GST law relating specifically to the treatment of government grants. Grant arrangements vary widely in their purposes, structure and the nature of the conditions they impose; for this reason, no blanket statement can be made as to the 'standard' treatment of government grants for purposes of GST. The GST consequences of making any particular grant will depend upon the character and circumstances of the grant in question, as determined by applying the general rules of the GST. The ATO is responsible for the interpretation and administration of the GST law, and provides interpretative advice to taxpayers on the application of the GST rules and principles to specific factual situations.

There are some particular cases in which the GST rules make it clear that the grantee is not making a taxable supply to the government agency providing the grant. Three such cases are:

- where a grant takes the form of a gift to a non-profit body;¹⁶⁰
- where, regardless of the characteristics of the recipient, a grant takes the form of an outright gift that imposes no conditions or obligations on the grantee;¹⁶¹
- where grant payments made between government entities (such as by the Commonwealth to a State government) are specifically covered by an appropriation.¹⁶²

In other cases, the grant may not be consideration for a supply to the government agency but rather consideration for a further or different supply made by the grantee to a third party recipient. Where the grantee makes a taxable supply to a third party the grantee would still be required to remit GST; alternatively, where the grant arrangement involved a GST-free supply or input-taxed supply, the grantee would not be required to remit GST.

As far as possible, business and government entities receive identical treatment under the GST law.

158 *A New Tax System (Goods and Services Tax) Act 1999*, Section 9-5

159 *A New Tax System (Goods and Services Tax) Act 1999*, Section 9-10

160 *A New Tax System (Goods and Services Tax) Act 1999*, Section 9-15 (3)(b)

161 Under the classification criteria discussed in Chapter 2, such an arrangement would in future be classified as a 'gift' rather than a 'grant' for purposes of the Commonwealth's financial framework.

162 Under *A New Tax System (Goods and Services Tax) Act 1999*, Section 9-15 (3)(c), such payments are specifically excluded from the definition of 'consideration'.

Government agencies, like business entities, charge GST on their commercial operations and claim input tax credits for their creditable acquisitions, including acquisitions made for the purpose of delivering policy objectives. It would be inappropriate, and inconsistent with broader government policy, to introduce specific rules for supplies where consideration takes the form of a government grant. It would also introduce further complexity into the law, given the need to ensure that the ordinary government procurement of goods and services remains taxable.

ISSUES

Improvements in program planning and design

A major contributor to confusion around the taxation treatment of grants, and hence a source of pressure to change that treatment, is the fact that taxation issues have often not been addressed at the time of the design, development and approval of new grant programs. The result has been a lack of clarity – including in publicity materials and application forms – as to whether grants are being provided on a pre-tax or post-tax basis. Uncertainty also arises as to the GST treatment of the grant. A consequence of this, in some cases, has been that grant recipients have complained to the Government when it becomes clear that their grants will be subject to tax, and that their net receipt will therefore fall short of what they had expected from the announcement. The Government in turn has come under pressure to provide additional funding to compensate for the effects of taxation on the value of the grant.

In a recent case involving the Tasmanian Forest Industry Development and Assistance Programs, the then Minister for Fisheries, Forestry and Conservation wrote to successful applicants in October 2007 – more than two years after the original decisions had been taken and announced – to advise that all grants awarded under the programs would be increased by 30 per cent to mitigate the tax consequences resulting from receipt of the original grant.¹⁶³ A similar gross-up had previously been provided for the restructuring of the fishing industry in Queensland. In both cases, the grant recipients in question were still able to claim tax deductions to the extent that their grants had been used on business-related expenditure; in this sense, the gross-up provided a double benefit to recipients, and the ultimate total value of the grant was arguably greater than the Government had originally intended.

In another recent case a Commonwealth agency ‘grossed up’ the payments it made under a large-scale community grants program on the understanding that the grants involved a taxable supply and were therefore subject to GST. Subsequently, however, it transpired that the program did not involve a consideration for a taxable supply made by the grant recipient, and that the funds were therefore outside the scope of GST.¹⁶⁴

163 Australian National Audit Office, *Tasmanian Forest Industry Development and Assistance Programs* (Audit Report No. 26 of 2007–08).

164 In this case, the conditions attaching to the program included requirements to spend the grant on specified purposes, to repay the funds in certain circumstances and to provide an acquittal for the funds. It transpired, however, that these conditions taken on their own were not sufficient for the grant to constitute consideration for a taxable supply: if nothing material passed back to the grantor, no consideration was involved and there was no requirement for the recipient to remit GST.

The Review considers that, in future, the expected taxation treatment of a particular grant should be an integral part of the planning and design of any new grants program, rather than a matter for subsequent consideration and *post hoc* adjustment of the funding base. The framework for submission of new policy proposals for grant programs should require proponents to deal explicitly with taxation issues¹⁶⁵: in particular, whether the grant is likely to be included in assessable income, whether GST is expected to apply, and the level and timing of net benefit intended to be payable (in aggregate), exclusive of GST. As far as possible, the costing of new policy proposals should also take these considerations into account. Once a decision has been taken on a new policy proposal, the terms of any government announcement on a new grant program should include a reference to the expected taxation treatment of the grants.

Consultation with the ATO

To assist in their consideration of the taxation implications of grants, agencies should consult with the ATO in the early stages of designing a new grant program. This is particularly important in the case of complex grant arrangements, or where there is any room for doubt as to the likely taxation status of a grant (for example, whether the grant represents a 'consideration for supply' for GST purposes). It is also good practice more generally, and should lead to greater clarity on the taxation treatment of grants than has been typical in recent times.

In most cases, there will be a benefit for all stakeholders if the agency delivering the program seeks a class ruling¹⁶⁶ from the Commissioner of Taxation, after the grant program structure has been finalised. This offers a means of providing transparency, additional certainty on taxation issues and more helpful guidance to potential applicants and grant recipients. It in no way fetters taxpayers in receipt of a grant from seeking a private ruling from the Commissioner. It would also enable the Commissioner to consider the possible need for amendment to Tax Pack and call centre advice.

Program documentation and publicity

In the process of developing a grant program, agencies will normally produce a range of documents, such as program guidelines, brochures, fact sheets and website materials, which provide information to potential applicants on the details of the program. In many cases such documentation offers no information on tax issues and, even where tax does rate a mention, it is often in the form of a standard reference to the need to seek professional advice on the tax implications of a grant. While this approach is understandable, it is also unhelpful.

It is virtually impossible to provide definitive advice covering every eventuality and individual circumstance, but a more generic statement about the expected taxation status of the grants in question should assist in raising awareness about the tax consequences of grants. The terms of such a statement should incorporate a reference to any class ruling on the grant program in question, and be one of the matters on which agencies consult with the ATO. Likewise, as far as possible, the expected GST treatment of the grant program should be made explicit in program documentation and publicity materials.

165 To the extent possible, having regard to the likely tax profile of intended grant recipients.

166 The Commissioner of Taxation cannot provide GST advice in a class ruling. However, the Commissioner could, if requested, provide written advice to the administering agency about the GST consequences of a grant arrangement.

Facilitation of agency requests for taxation advice

The line agencies consulted in the course of the review generally acknowledged that taxation had been a 'problem area', and were broadly supportive of the directions of change outlined above. At the same time, however, a number of agencies expressed a concern that a requirement to consult with the ATO at the program design stage could lead to extensive and possibly unacceptable delays, especially if a large volume of requests for ATO advice or rulings were to be made by a range of different agencies more or less simultaneously.

The Review understands this concern, and acknowledges that it represents a risk to be managed; at the same time, however, it holds firmly to its view that the expected taxation treatment of a new grant program should be an integral part of program planning and design, and that agencies should consult in that process with the ATO as the authoritative source of information and advice on taxation matters. In recognition of the issues raised by line agencies, and given Finance's role as the whole-of-government coordinating agency for grants policy and administration, the Review suggests that Finance should work with the ATO to ensure that agency requests for advice on the taxation treatment of grant programs can be processed promptly and efficiently.

Recommendation 20

The Review recommends that:

- (a) the expected tax treatment of grants should be a matter for explicit consideration in the planning and design of any new grant funding program. The framework for submission of new policy proposals for grant programs should require proponents to deal explicitly with taxation issues, and the terms of any government announcements on new grant programs should include a reference to the expected taxation treatment of the grants;*
- (b) agencies should be required to consult with the Australian Taxation Office in the process of designing a new grant program. The objective would be to provide additional certainty regarding the expected taxation treatment of grants, and more helpful guidance to potential applicants and grant recipients;*
- (c) in developing their program documentation and publicity materials for a grant program, agencies should incorporate an explicit reference to the expected taxation status of the grants in question. The terms of this statement should be developed in consultation with the ATO, and include reference to the GST status of the grants and any class ruling obtained from the Commissioner of Taxation; and*
- (d) Finance should work with the ATO to ensure that agency requests for advice on the taxation treatment of grant programs can be processed promptly and efficiently.*

Taxation status of grants

As discussed above, most government grants are currently subject to taxation to the extent that they fall within the scope of general taxation law. Allowing for the wide differences in the characteristics of grant programs and the circumstances of grantees, this is equitable from the point of view of treating like with like and ensuring that, where a grant takes the form of income, it is treated and taxed as such.¹⁶⁷

In a small minority of cases previous governments have taken the view that certain grants should be specifically exempt from tax, and have enacted legislation to this effect. The Review is not convinced that this approach is necessary, in some cases, or appropriate, in others. In many cases, the tax liability arising from a grant can be offset against deductions which are derived from other expenditure. In the case of grants paid for industry restructuring (such as those in the dairy and sugar industries), the exemption from tax means that all grant recipients receive an identical value of grant, despite potentially large differences in their other sources of income and broader financial circumstances. A more equitable approach would be to make the grants taxable, but to consider the average tax rate of likely recipients when determining the size of the grant.

On these grounds, the Review questions the need to exempt grants specifically from tax. As a matter of general principle and standard practice, it considers that grants provided under Commonwealth funding programs should be subject to taxation to the extent that their characteristics place them within the scope of general taxation law.

A related issue concerns the way in which grants are structured and administered. In one recent case, a Commonwealth agency responsible for a large grant program sought to structure some substantial grants to a Government Business Enterprise with the specific objective of ensuring that the company would not be required to pay income tax on the grants. In order to achieve that objective, the agency arranged for the grants to be paid on a totally untied basis, with the projects to be funded selected solely by the company in question. Moreover, no contracts, funding agreements or documented governance arrangements were put in place that would ensure that the grant funding was applied to the purposes approved by Ministers, or in any particular timeframe.¹⁶⁸

Arrangements along these lines are inappropriate on several counts: not least, because they put the interests of the grant recipient above the interests of the Commonwealth, and fail to ensure that funds are applied to their intended purposes. Any new policy framework for the administration of grants should address such matters, and specifically prohibit the structuring of grant arrangements with the objective of removing or minimising the regular tax obligations of a recipient.

167 A high proportion of the Commonwealth's 'discretionary grants' in 2007 were awarded to community service organisations, charitable institutions, educational organisations, health organisations, cultural organisations, sporting organisations or other non-profit organisations which are either actually or potentially exempt from income tax (see Attachment B).

168 Australian National Audit Office, Administration of Grants to the Australian Rail Track Corporation (Audit Report No. 22 of 2007–08).

Recommendation 21

The Review recommends that, as a matter of general principle and standard practice, grants provided under Commonwealth funding programs should be subject to taxation to the extent that they fall within the scope of general taxation law. Where tax is potentially payable on a grant, the new policy framework for the administration of grants should explicitly prohibit the structuring of grant arrangements with the objective of removing or minimising the regular tax obligations of a recipient.

'Grossing up' of grants for GST

Where a grant arrangement involves a taxable supply, for which the grant is consideration, a grantee registered or required to be registered for GST will be required to remit GST. In these circumstances, an administering agency will often 'gross up' the grant by 10 per cent in order to cover the grantee's GST liability and thereby provide the level of net benefit intended. The Review considers that this is an appropriate arrangement in those cases where, following consultation with the ATO, an agency has reason to believe that the grant payment will be subject to GST. Section 30A of the *FMA Act 1997* provides a mechanism which allows agencies to finance the GST component of such payments without recourse to additional funding through the Budget process.

Where an agency considers it likely that some grant recipients will not be registered, or required to be registered, for GST, the issue arises as to whether the level of grant payment should be adjusted so that the 'gross-up' component is removed. The case for such adjustment will depend on a range of risk-related considerations: among them, the target group for the program; the proportion of grant recipients likely not to be registered for GST; the amounts of funding involved; and the costs associated with collecting and processing data on the GST registration status of individual applicants. Where the number of non-registrants is likely to be low, relative to the total number of grants awarded, and subject to the other considerations mentioned, it should be open to an agency to pay all grants on a grossed-up basis, irrespective of the GST registration status of any particular grantee. This would be subject to the requirement that all grant funds should be applied to agreed purposes, as defined in the relevant program guidelines and funding agreement.

Recommendation 22

The Review recommends that, where consultation with the ATO indicates that a grant arrangement will be subject to GST, the administering agency should 'gross up' the value of grants paid to GST-liable grantees by 10 per cent in order to cover their GST liabilities and thereby provide the level of net benefit intended. Where justified on the basis of a documented risk assessment, it should be open to an agency to pay all grants within a program on a grossed-up basis, irrespective of the GST registration status of any individual grantee.

09

CHAPTER NINE: IMPROVING EFFICIENCY IN GRANTS ADMINISTRATION



This chapter deals with a range of efficiency issues related to the administration of grant programs. Consistent with the terms of reference, it proposes a number of measures designed to streamline program structures and related administrative processes, reduce unnecessary burdens on grant recipients and cut red tape. It recommends also that the large number of grant management systems in use across the Commonwealth be reviewed and rationalised with a view to delivering better services, reducing costs and improving efficiency. The Review considers that significant savings could accrue, over time, from these measures.

Streamlining program structures

Chapter 6 drew attention to the large increase in the number of discretionary grant programs over recent years and the haste with which many such programs have been put in place. Even on the partial evidence of the Discretionary Grants Central Register, there are now some 250 separate grant funding programs across the Commonwealth, each with its own program guidelines, advertising budget, selection and assessment procedures, funding agreements, payment and acquittal arrangements, monitoring and assessment procedures, and associated administrative costs. On the surface, at least, many of these programs appear strikingly similar in their stated purposes and intended target groups.

In the haste with which many grant programs have been developed and implemented, the question has too rarely been asked as to whether an existing program could be expanded or modified to meet an identified need: rather, new programs have been established – often without adequate planning, as discussed in Chapter 3 – and the total number of programs has been allowed to grow with little sense of overall strategy or control.¹⁶⁹ In the Review's judgement, it is timely to take stock of the array of grant programs now in place and, over and above any judgements made on the effectiveness of those programs, to assess the case for streamlining, simplification and rationalisation. The potential value of such a process is well illustrated by a recent example.

In 2006, the then Minister for Families, Community Services and Indigenous Affairs asked his department to review the structure of its community services grant programs and to identify opportunities for streamlining and simplification. The aim was to reduce complexity and duplication in the department's administered items structure by bringing together those grant programs with similar purposes. Several important changes and benefits flowed from this process of review:

- > The number of separate community services grant programs was cut from 48 to 24 – a 50 per cent reduction – without compromise to program objectives or to the purposes for which funds were appropriated. The change in FaHCSIA's program structure was reflected in its 2007–08 Portfolio Budget Statement.
- > In the case of the remaining 24 programs, changes were made where necessary to better reflect the underlying purpose of the relevant appropriations. In consequence, there is now a clearer sense of the distinct purposes served by separate programs, and of how they relate one to the other. Among other benefits, this has assisted in providing better and clearer information to stakeholders, applicants and grant recipients.

¹⁶⁹ Various factors have contributed to this growth in the size and complexity of program structures. Political factors have played a part (e.g., the attraction of announcing a new program, even if an existing program serves the same or a very similar purpose), but also structural factors (e.g., machinery of government changes, which have rarely involved any significant rationalisation of pre-existing program structures).

- > The more streamlined and coherent program structure has facilitated some significant improvements in performance reporting. High level 'program logic statements' have been developed for each new administered item, and a standard performance framework now applies across the full range of FaHCSIA's community-based programs. The number of grant performance indicators has been reduced by some 78 per cent (from 286 to just 62), and the quality of indicators improved, without loss of essential information or compromise to data integrity.¹⁷⁰
- > Administrative support and overhead costs are being reduced significantly (and savings thereby achieved), reflecting the removal of duplication and the reduction in the number of separate 'programs' to be managed. The resources freed by program streamlining are now being used in more productive ways – in particular, in improving the quality of service delivery and supporting the achievement of program outcomes.

It may reasonably be asked whether 24 separate grant programs catering for the community services sector within the one portfolio is more than necessary; indeed, FaHCSIA itself has concluded that further streamlining of its program structures is both possible and desirable. Even on the evidence of the work undertaken to date, however, it is clear that there is both significant potential for program streamlining and simplification and major benefits to be gained from a well-designed and comprehensive process of review. The Review proposes that all grant-administering agencies should be encouraged to conduct a review along these lines.

Recommendation 23

The Review recommends that:

- (a) *grant-administering agencies be encouraged to review the structure of their grant programs with a view to reducing the overall number of programs, achieving greater coherence and clarity of objectives, improving transparency, reducing but sharpening the range of performance indicators, and achieving administrative savings; and*
- (b) *agencies be asked to report on the results of the review at (a) in the context of the 2009–10 Budget.*

Review of grant management systems

A Finance survey conducted early in 2006 found that there were at least 164 separate grant information systems in operation across the Commonwealth.¹⁷¹ Most of these systems were either 'home-grown' (54 per cent) or 'other' (paper-based, spreadsheet and Word systems; 37 per cent); the remaining fifteen systems (9 per cent) were off-the-shelf acquisitions, 12 of which had been customised to meet particular agency needs. While most agencies operated fewer than 10 systems, four agencies had a total of 115 systems between them – an average of 29 per agency – and these accounted for some 70 per cent of the total number of systems reported. More than half of all systems were maintained by a program team within the reporting agency.

170 Based on information supplied by FaHCSIA. The department is currently considering the case for implementing a standard performance framework across all its programs, including income support and specific purpose payments programs.

171 Australian Government Information Management Office (AGIMO), *Report to CIO Committee on Survey of Australian Government Agencies' Use of Grant Management Systems*, February/March 2006. The survey covered 99 agencies, of which 68 provided responses and 25 reported that they had implemented grant management systems.

There were some clear limitations on the functionality of the systems reported. Only 35 systems (21 per cent) were web-based, and just 47 (29 per cent) covered the full 'life cycle' of grants, covering the processes of notification, applications, assessment and approval, announcement, grant management and monitoring, and wind-up and evaluation. More than half of agencies reported that they were unable to obtain consolidated management information across different grant programs without significant manual effort, and only 12 per cent of systems were able to transfer data to the agency's financial system. There was limited cross-agency collaboration in the development or use of grant management systems.¹⁷²

Although the Review is not in a position to make any detailed judgements in this area on its own account, the evidence provided by the Finance survey gives cause to question both the efficiency of the IT system arrangements supporting the operation of Commonwealth grant programs and the likely quality of many of those systems. The Review notes that, as part of his current examination of the Commonwealth's use and management of information and communication technology, Sir Peter Gershon has been asked to advise on:

- > *the possible duplication of ICT systems across government agencies, whether opportunity exists to consolidate existing or new systems, and what form any consolidation should take; and*
- > *the duplication of business processes across, and within agencies, and the effects this has on costs to government and the quality of service delivery.*¹⁷³

To help inform its work, the Gershon Review is conducting a survey of ICT expenditure and operations across FMA Act agencies, and as part of that survey, has sought detailed data on agencies' current use of grant management systems.

There is an obvious relationship between this set of issues and the previous discussion of grant program structures, in that the number of separate grant management systems is closely related to the number of different grant programs to be managed: to the extent that program streamlining can reduce the latter number, there should be a corresponding reduction in the number of grant management systems required. Desirably, also, this would create scope for improvements in the quality and consistency of the remaining ICT systems.

Subject to the Government's decisions on the findings of the Gershon Review, a sensible way of proceeding in this area would be for Finance to lead a process designed to review and rationalise the number of grant management systems in use across the Commonwealth. The objectives of this review would be to deliver better services, promote more consistent business processes, increase the portability of information across different systems, reduce software development and maintenance costs, and achieve administrative savings more generally.

172 *ibid.*

173 *Review of the Australian Government's use of Information and Communication Technology (Gershon Review), Terms of Reference*

So as not to compromise legitimate agency-specific or program-specific needs, any review along these lines should be conducted in close consultation with line agencies. A first step would be to ask the Business Process Transformation Committee¹⁷⁴ to determine standard business process patterns for grants management across agencies, as a basis for defining system requirements and specifications. In the longer term, the objective should be to authorise a small number of software platforms which meet most, if not all, the grant management system requirements of Commonwealth agencies; within this set, agencies should be free to choose the particular program best suited to their needs, with some flexibility also to adapt the platform chosen to meet particular agency business requirements.

Recommendation 24

The Review recommends that, subject to Government decisions on the findings of the Gershon Review:

- (a) the number of grant management systems in use across the Commonwealth be reviewed and rationalised with a view to delivering better services, promoting consistent business processes, increasing the portability of information across different systems, reducing software development and maintenance costs, and improving efficiency more generally;*
- (b) the review recommended at (a) should be led by Finance but conducted in close consultation with agencies;*
- (c) as a first step, Finance should work in partnership with relevant line agencies, through the Business Process Transformation Committee, to determine standard business process patterns for grants management across agencies; and*
- (d) in the longer term, the objective should be to authorise a small number of software platforms which meet most, if not all, the grant management system requirements of Commonwealth agencies; within this set, agencies should be free to choose the particular program best suited to their needs, with some flexibility also to adapt the platform chosen to meet particular agency business requirements.*

Cutting red tape within government

An important means of improving the efficiency of grant program administration is by eliminating unnecessary processes and cutting red tape. The most significant and useful step that could be taken in this direction would be to reduce the total number of separate grant programs by culling redundant or ineffective programs and streamlining program structures, along the lines proposed in Recommendation 23. Such a measure could markedly increase administrative efficiency and generate substantial savings; moreover, to the extent that it helped to clarify objectives, reduce paperwork and ease the burden of reporting and acquittal processes, it would also be welcomed by many grant recipients.

¹⁷⁴ The Business Process Transformation Committee (BPTC) is a group of senior executive officers (mostly at Deputy Secretary level) responsible for transforming the way that Commonwealth agencies do business through ICT with a view to improving service delivery. Serviced by AGIMO, the BPTC is chaired by the Australian Government Chief Information Officer and reports to the Secretaries' Committee on ICT. Its membership currently comprises senior officers drawn from the Australian Taxation Office, Centrelink, the Department of Defence, the Department of Human Services, the Department of Immigration and Citizenship, the Department of Innovation, Industry, Science and Research, the Australian Bureau of Statistics, the Australian Public Service Commission, the Department of Education, Employment and Workplace Relations and the Department of the Prime Minister and Cabinet. Other members may be co-opted as business requires.

In addition to the streamlining of program structures, the Review has identified significant scope to improve the efficiency of whole-of-government processes covering the administration of grant programs. Key measures recommended in this regard include:

- > the development of better central guidance on definitions, classifications and grants policy issues (Recommendations 1–3);
- > significant changes to planning and decision-making arrangements, designed to clarify key responsibilities and accountabilities (Recommendations 6–11);
- > replacement of the requirement for ERC consideration of detailed program guidelines with a more efficient, assurance-based process (Recommendation 6);
- > abolition of the requirement to seek the Finance Minister's approval for the the introduction of a new and more efficient reporting system for grants, better connected to agencies' information systems (Recommendation 12);
- > the dismantling of current grant reporting systems, once the new reporting system is operating efficiently and effectively (Recommendation 14(a) and (b));
- > the review and rationalisation of whole-of-government reporting requirements in relation to grants (Recommendation 14(c) and (d));
- > improvements in performance measurement and assessment processes (Recommendation 18); and
- > a review and rationalisation of grant management systems across the Commonwealth (Recommendation 24).

In combination, these measures should substantially increase the efficiency of current administrative processes and, over the medium term, generate significant savings in departmental expenses.

Recognising that the full implementation of Government decisions on these matters is likely to take a number of years, the Review proposes that an implementation strategy and transition plan should be developed which identify the appropriate staging and sequencing of particular measures. In developing this plan, priority should be given to practical measures which will improve the efficiency of current administrative processes, consistent with the broad directions proposed in this report. The Review sees no good reason, for example, why the current approval requirement governing the award of multi-year discretionary grants should not be abolished forthwith. Likewise, while it recognises that the Discretionary Grants Central Register will need to remain in place for the time being, as the only source of whole-of-government information on discretionary grants, it suggests that reporting arrangements for this purpose could be reviewed and streamlined with a view to reducing the current heavy reporting burden on agencies. A practical step in this direction, for example, would be to limit the reporting requirement to those grants for which a funding agreement has been signed.¹⁷⁵

175 Apart from other benefits, this would simplify the reporting process for agencies and improve the quality of financial data reported (by ensuring consistency between the details reported on the DGCR and the terms of the relevant funding agreement).

Recommendation 25

The Review recommends that, once Government decisions have been taken on the outcomes of this review:

- (a) Finance develop and circulate to agencies an implementation strategy and accompanying transition plan;*
- (b) in developing the transition plan at (a) above, priority be given to practical measures which will improve the efficiency of current administrative processes, both at whole-of-government level and within particular agencies; and*
- (c) as one transitional measure, Finance review the details of its current reporting requirements in relation to the Discretionary Grants Central Register, with a view to improving efficiency and reducing the reporting burden on agencies.*

Cutting red tape for grant recipients

It is important also to consider the needs and interests of grant recipients: too often in the past this important perspective has been either overlooked or downgraded in the design and administration of the Commonwealth's grant programs. With community-based and other non-profit organisations accounting for a high proportion of all grants awarded by the Commonwealth in recent years,¹⁷⁶ particular attention should be paid to the needs of this sector.

The Government has acknowledged the important role played by the community and voluntary sector in meeting the needs of disadvantaged Australians, and in promoting its broader social inclusion objectives. In recognition of that role, it has made a number of commitments designed both to strengthen the sector and improve the quality of its relationship with government. Specific measures announced in this direction include:

- > a commitment to remove 'gag clauses' from government contracts with the voluntary sector;¹⁷⁷
- > a commitment to cut unnecessary red tape, including 'layers of imposed bureaucratic reporting', from grant agreements;¹⁷⁸ and
- > an intention to enter into a 'national compact' with the community sector, defining a set of common goals and a timetable for addressing key issues of mutual concern.¹⁷⁹

The Review has been mindful of these commitments in developing its proposals and recommendations for change. In the important area of funding agreements, for example, it has recognised that many funding agreements in the past have been unduly long and complex documents, and unnecessarily onerous in their demands on grant recipients. For the future, it has proposed that the form of funding agreement to be used in any particular case should be based upon the principle of 'proportionality'; that agreements should be cast in plain English as far as possible, with a minimum of complexity and

177 See data at [Attachment B](#).

177 The Hon. Julia Gillard MP, Minister for Social Inclusion, *Media conference*, Melbourne, 9 January 2008. 'Gag clauses' were clauses inserted into government contracts which prevented a funding recipient from making certain public statements without prior notice to the government.

178 Senator the Hon. Ursula Stephens, Parliamentary Secretary for Social Inclusion and the Voluntary Sector, *Speech to the ACOSS Conference*, Melbourne, 9 April 2008

179 *ibid.*

legal jargon; and that funding agreements for small-scale, one-off grants should generally take the form of a simple letter of offer, with detailed conditions kept to a minimum (Recommendations 16 and 17). As the Government has acknowledged, a fine balance needs to be struck in these matters:

“.....grant-makers and grant-seekers may share the same aspirations but can have very different perceptions on how these aspirations can be met..... Appropriate and effective accountability mechanisms are needed which do not prevent organisations from delivering vital services.”¹⁸⁰

Detailed judgements on the application of the ‘proportionality’ principle will usually be made at the program level within particular agencies, and it is at this level that a sensitivity to the circumstances and interests of grant recipients is most important. The recent restructuring of FaHCSIA’s Volunteer Small Equipment Grants (VSEG) program was driven partly by efficiency considerations, given the high volume of applications received (up to 15,000 per year) and the need to streamline the department’s administrative processes; at the same time, however, a conscious effort was made to structure the new arrangements in ways which would make life easier for the non-profit community organisations which are the recipients of funding under this program. The new program arrangements now include, for example:

- > a telephone hotline and email mailbox service;
- > online advertisement of program guidelines and application forms;
- > the opportunity for online submission of grant applications (with the application form provided as an easy-to-use ‘fill and submit’ PDF);¹⁸¹
- > online assessment of applications received, in the interests of both speed and consistency of assessment;
- > use of a simple form funding agreement, mass produced online (along with letters to all unsuccessful applicants);
- > provision for the acceptance of funding agreements by return email; and
- > electronic payment of grant funds to successful applicants.

These new arrangements have been well received by applicants and grant recipients, while at the same time delivering major efficiency benefits to the department. The use of online application and assessment tools, in particular, offers major benefits both to administering agencies and to grant applicants, and should be one of the matters considered in the design of the new whole-of-government reporting system recommended in Chapter 4.¹⁸²

A common criticism of government arrangements for the administration of grants has been the assumption that the same approach will suit all circumstances, regardless of the scale or purposes of the grant in question or the performance record of the grant recipient. The volume, detail and frequency of reporting obligations have been a particular focus of criticism in this regard.¹⁸³

180 Senator the Hon. Ursula Stephens, Parliamentary Secretary for Social Inclusion and the Voluntary Sector, Parliamentary Secretary Assisting the Prime Minister for Social Inclusion, *Speech to The PricewaterhouseCoopers Transparency Awards*, Sydney, 17 April 2008

181 In the latest VSEG selection round, about 75 per cent of all applications were submitted online.

182 The online grants system used by the United States Government (www.grants.gov) provides not only a single source of information on federal grant funding opportunities but also a portal through which grant applications can be submitted. Of the 25 agencies which responded to the AGIMO survey of February/March 2006, 13 had systems which allowed applicants to apply for grants online. In six of these cases, applicants could also monitor the progress of their applications online; in six further cases, grant recipients could report online on their performance under the funding agreement.

183 Commissioner Susan Pascoe AM, State Services Authority, Victoria, *Reducing Red Tape: Easing the administrative and compliance burden to achieve better results*, Best Practice in Grants Administration Conference, Melbourne, 29 February 2008.

The Review accepts that there is some substance in such criticisms, and its recommendations on funding agreements in particular acknowledge the need to strike a new balance, based on a more measured assessment of risk. In line with this approach it suggests that, where grant funding is used to support the ongoing delivery of services from the same organisations over a period of years, agencies should be encouraged to adjust the detail of their accountability and reporting requirements in line with a provider's established record of compliance and performance. Subject to transparency considerations and risk management principles, for example, it is reasonable to expect that service providers with consistent records of high performance and reliability should be able to 'earn' lighter-touch accountability requirements and a greater measure of autonomy, relative to other providers without an established record of performance.

These judgements will best be made at the agency level, with appropriate documentation of reasons. Decisions taken in this area should periodically be subject to review, so that accountability and reporting requirements remain well aligned to considerations of performance and risk.

Recommendation 26

The Review recommends that, where grant funding is used to support the ongoing delivery of services from the same organisations over a period of years, agencies should be encouraged to adjust the detail of their accountability and reporting requirements in line with a provider's established record of compliance and performance. Subject to transparency considerations and risk management principles, service providers with consistent records of high performance and reliability should be able to 'earn' lighter-touch accountability and a greater measure of autonomy, relative to other providers without an established record of performance.

ATTACHMENTS



ATTACHMENT A: TERMS OF REFERENCE

Government agreed that the Department of Finance and Deregulation (Finance) would undertake a comprehensive strategic review of the administration of grants programs with the recommendations of the review to be provided to the Government in 2008. The review will examine the adequacy of current administrative processes and recommend to the Government measures to improve the framework for the administration of Australian Government grants.

The proposed purpose, scope, conduct and timeline for the review are outlined below.

Affected agencies: The Department of the Prime Minister and the Cabinet (PM&C); the Department of the Treasury (Treasury); Finance; and other line agencies that manage Australian Government grants programs.

Purpose

The objective of the strategic review is to improve the administration of grant programs with a particular view to improve efficiency, effectiveness, transparency, and accountability. The review will also assess the merit of discretionary grants as a vehicle for delivering some or all aspects of Government policy.

The review will make recommendations for improving the framework for the administration of Australian Government grants and to identify better practice in the administration of Australian Government grants.

The review will comprise of two elements which will be conducted in parallel:

- > The first element will examine the adequacy of current administrative processes and make recommendations for improving the overall framework for the administration of Australian Government grants to identify better practice in the administration of Australian Government grants. Included in this element will be a process to disseminate the outcomes of the review to all agencies and assist agencies with aligning their grant programs with the improved framework for the administration of Australian Government grants.
- > The second element is a discrete assessment of the merit of discretionary grants as a mechanism for delivering Government policy. The review will also consider possible options to measure, over time, the longer term benefits of using discretionary grants as a funding mechanism for Government.

Scope of the review

First Element

The first element of the review will examine the adequacy of the current administrative processes for all types of Australian Government grants programs and recommend improvements to policies for the administration of grant programs.

Grants are non-reciprocal transfers of resources from the Australian Government to other entities which may or may not be subject to unilaterally imposed conditions. This definition of grants programs excludes procurement activity and transfer payments (for example, income support payments).

The review will recommend improvements to whole-of-government policies for the administration of grant programs by:

- > defining the broad categories of grant programs including discretionary grants and identifying the appropriate administrative arrangements for each of these categories;
- > reviewing and recommending improvements to the appropriate transparency, disclosure requirements and reporting for each category of grant program;
- > identifying and recommending the appropriate roles and responsibilities for ministers (including for any delegated powers), agencies, and other decision-making bodies in the administration of grants programs;
- > identifying and recommending the appropriate forms for grant agreements (contracts/funding agreements), taking into account both the size of the grant and reciprocity required;
- > identifying and recommending the appropriate arrangements for the measurement and assessment of the performance of grant projects and grant programs;
- > identifying problems in the application of the accounting treatment for different categories of grants under both the Australian Accounting Standards and the Government Finance Statistics and how compliance can be improved;
- > reviewing how the various types of grant payments are treated under the relevant tax laws and the *Financial Management and Accountability Act 1997*, *Commonwealth Authorities and Companies Act 1997* (where relevant), other relevant legislation, and the implications including for grant recipients;
- > reviewing and recommending the basis for determining the taxation treatment of grants; and
- > recommending options for streamlining, reducing red tape, administration costs and/or regulations for both government agencies and grant recipients and any necessary improvements to the way grants are recorded to improve transparency and the monitoring of decisions.

Following Government's consideration of the outcomes of the review, it is anticipated there may be changes to the administration of grant programs. The review team will work with agencies to ensure their grants programs align with the improved framework for the administration of Australian Government grants.

Second Element

The second element of the review will assess the merit of discretionary grants as a mechanism for delivering Government policy; this will include considering possible methods to measure, over time, the longer term benefits of using discretionary grants as a funding mechanism. In doing this the review will:

- > review the advantages and disadvantages of discretionary grants as a funding mechanism including for different customers and different expenditure objectives;
- > review international best practice, adapting principles for use in the administration of discretionary grants in Australia;

- > review the merit of past significant growth in the number and value of discretionary grants provided by the Australian Government;
- > review alternate ways of achieving program outcomes other than through discretionary grants;
- > review the appropriateness and effectiveness of providing ad hoc discretionary grants;
- > review best practice in the performance management of discretionary grants, particularly the measurement of outcomes; and
- > review the long term effectiveness and benefits of discretionary grants.

Methodology

The review will draw on:

- > work already undertaken for the previous review of discretionary grants;
- > consultations with agencies with grants programs, and with the consultative group;
- > previous reviews, reports and audits, whether internal or external, or public or unpublished, and the *Discretionary Grants Register User Manual*;
- > agency arrangements for Australian Government grants programs; and
- > processes and procedures for grants program administration by other governments (both Australian and international).

Deliverables

A report on the first element of the review will be provided to the Minister for Finance and Deregulation (Finance Minister) by June 2008 and the report on the second element will be provided to the Finance Minister by July 2008.

Responsibilities and Governance

The review will be undertaken under the Strategic Review Framework.

The first element of the review will be led by Mr Peter Grant PSM.

The second element of the review will be conducted by Dr Joanne Kelly, University of Sydney, in liaison with Mr Grant so as to provide continuity for the review and to avoid unnecessary duplicate requests for information from agencies.

Coordination and monitoring of the review's progress will be undertaken by the Strategic Review Unit in Finance.

Consultation

Consultative Group

Membership: PM&C; Finance, Treasury, Department of Families, Housing, Community Services and Indigenous Affairs, Department of Infrastructure, Transport, Regional Development and Local Government and the Australian Research Council.

A consultative group will be established to discuss issues raised by the review, and provide input to the review. The consultative group will be chaired by the First Assistant Secretary, Financial Framework Division, Finance.

Consultation with line agencies

The reviewers will undertake bilateral consultation with relevant agencies during the review process. The reviewers may provide draft copies of discussion papers or the review reports to line agencies for comment. Agencies will be updated on the progress of the reviews through the Chief Financial Officer Forum.

Confidential consultation with external stakeholders may also be conducted if required.

Overview Timeline – Strategic Review of Grants Administration

Event	Date
The reviewer of the first element & review team commence work	Mid-February 2008
Analysis of grant programs, existing reviews and state of play	Late February-April 2008
Consultation with stakeholders	
Development of draft findings/recommendations/report	
Academic for second element engaged and work commences.	Mid-March 2008
Provision of draft findings/recommendations/report for both elements to stakeholders	Early May 2008
Consultation with stakeholders on the draft provided	
Report of the first element finalised and provided to Finance Minister	June 2008
Report of the second element finalised and provided to Finance Minister	July 2008
Proposal of improvements to the framework for the administration of grants to be considered	July-August 2008
The review team works with agencies to ensure their grant programs align with the improved framework for the administration of Australian Government grants	July-October 2008
Guidance on the administration of Australian Government grants framework issued by Finance	October 2008 (following Government approval)

ATTACHMENT B: SUMMARY DATA ON COMMONWEALTH DISCRETIONARY GRANTS

The data reported below are all sourced from the Discretionary Grants Central Register. Any discrepancies between totals and sums of components are due to rounding.

Table 1: Distribution of Grants by Value of Grant, 2006 and 2007

Value of Grant	Number of Grants, 2006	Total Amount Approved, 2006 (\$'000)	Number of Grants, 2007	Total Amount Approved, 2007 (\$'000)	Variance, 2006–07 (Number of grants)	Variance, 2006–07 (Value of grants) (\$'000)
< \$1,000	463	300	2,433	1,780	1,970 (525%)	1,480 (593%)
\$1,001 – \$5,000	2,588	7,070	28,270	62,740	25,682 (1092%)	55,670 (887%)
\$5,001 – \$50,000	7,694	189,550	12,017	320,550	4,323 (156%)	131,000 (169%)
\$50,001 – \$500,000	3,025	488,610	4,945	810,850	1,920 (163%)	322,240 (166%)
\$500,001 – \$5m	703	1,081,470	1,277	1,745,230	574 (182%)	663,760 (161%)
> \$5m	66	948,420	118	1,608,750	52 (179%)	660,330 (170%)
Total	14,539	\$2,715,507	49,060	\$4,549,908	34,918	\$1,834,480

Note: Data for 2006 exclude an estimated 8,000 small-value sporting grants administered by the Australian Sports Commission.

Table 2: Distribution of Grants by Portfolio, 2007

Portfolio	Number of grants awarded	% of total	Value of grants received (\$'000)	% of total	Average value of grant (\$)
FaHCSIA	16,458	33.5	1,786,841	39.3	108,600
DEWHA	7,170	14.6	1,191,381	26.2	166,200
Health	14,637	29.8	785,095	17.3	53,600
DEEWR	6,562	13.4	267,546	5.9	40,800
DBCDE	118	0.2	119,070	2.6	1,009,100
Infrastructure	365	0.7	104,188	2.3	285,400
DAFF	545	1.1	103,039	2.3	189,100
AGD	1276	2.6	94,685	2.1	74,200
DIISR	28	0.1	36,931	0.8	1,319,000
Other	1901	4.0	61,132	1.2	32,200
TOTAL	49,060	100	4,549,908	100	92,700

Table 3: Distribution of Grants by Type of Recipient Organisation, 2007

Organisation type	Number of grants received	% of total	Value of grants received (\$'000)	% of total	Average value of grant (\$)
Community organisations (a)	25,008	51.0	1,710,063	37.6	68,400
Government organisations (b)	2,030	4.1	1,122,234	24.7	552,800
Indigenous organisations	2,765	5.6	1,014,637	22.3	367,000
Educational institutions	10,012	20.4	162,816	3.6	16,300
For-profit organisations	3,482	7.1	222,610	4.9	64,000
Sports-related bodies	2,558	5.2	35,389	0.8	13,800
Other, n.e.c. (c)	3,205	6.5	282,160	6.2	88,000
TOTAL	49,060	100	4,549,908	100	92,740

- (a) Includes organisations classified to the following categories within the Discretionary Grants Central Register: Church-based organisation; Community group; Non-profit organisation; Social service organisation.
- (b) Includes organisations classified to the categories of Commonwealth-controlled entity; Government organisation; and Local government organisation.
- (c) Includes organisations classified to the categories of Cultural organisation; Defence organisation; Health institution; Industry-related body; International organisation; Regional organisation; Research institution; Veterans' organisation; Women's organisation; and Other (no classification provided).

Table 4: Ten Largest Discretionary Grants Awarded, 2007

Portfolio	Grant Program / Recipient	Total Amount Approved \$
DEWHA	Water Smart Australia – Western Corridor Recycled Water Pty Ltd	408,000,000
DEWHA	Water Smart Australia – Gordon City Council	80,300,000
DEWHA	Water Smart Australia – NSW Department of Natural Resources	71,770,000
Health	Aboriginal and Torres Strait Islander Health – Central Australian Aboriginal Congress Inc	50,052,287
FaHCSIA	Community Housing and Infrastructure Appropriation – Aboriginal Housing Authority	40,014,300
DEWHA	Water Smart Australia – SA Water Corporation	34,500,000
DEWHA	Water Smart Australia – Department of Sustainability and Environment (VIC)	31,000,000
Health	Aboriginal and Torres Strait Islander Health – Nganampa Health Council	25,199,320
DEWHA	Water Smart Australia – Dept of Sustainability and Environment (VIC)	25,000,000
Health	Aboriginal and Torres Strait Islander Health – Nunkuwarrin Yunti Inc.	22,147,206

ATTACHMENT C: AUSTRALIAN NATIONAL AUDIT OFFICE: KEY AUDIT REPORTS ON GRANT PROGRAMS, 2004–05 TO 2007–08

Parent School Partnership Initiative
(Audit Report No. 29, 2007–08)

Emergency Management Australia
(Audit Report No. 27, 2007–08)

Tasmanian Forest Industry Development and Assistance Programs
(Audit Report No. 26, 2007–08)

Administering Round the Clock Medicare Grants
(Audit Report No. 25, 2007–08)

Administration of Grants to the Australian Rail Track Corporation
(Audit Report No. 22, 2007–08)

Performance Audit of the Regional Partnerships Programme
(Audit Report No. 14, 2007–08)

Australian Technical Colleges Program
(Audit Report No. 3, 2007–08)

Management of Pharmaceuticals Partnership Program
(Audit Report No. 46, 2006-07)

Distribution of Funding for Community Grant Programs
(Audit Report No. 39, 2006-07)

Administration of the Community Aged Care Packages Program
(Audit Report No. 38, 2006-07)

Administration of State and Territory Compliance with the Australian Health Care Agreements
(Audit Report No. 19, 2006-07)

National Food Industry Strategy
(Audit Report No. 11, 2006-07)

Administration of the Native Title Respondents Scheme
(Audit Report No. 1, 2006-07)

Management of Selected Telstra Social Bonus 2 and Telecommunications Service Inquiry Response Programs
(Audit Report No. 52, 2005–06)

Arrangements to Manage and Account for Aid Funds Provided Under the Australia-Indonesia Partnership for Reconstruction and Development
(Audit Report No. 50, 2005–06)

Funding for Communities and Community Organisations
(Audit Report No. 47, 2005–06)

Administration of Primary Care Funding Agreements
(Audit Report No. 41, 2005–06)

The Australian Research Council's Management of Research Grants
(Audit Report No. 38, 2005–06)

Administration of the R&D Start Program
(Audit Report No. 15, 2005–06)

Administration of the Commonwealth State Territory Disability Agreement
(Audit Report No. 14, 2005–06)

Provision of Export Assistance to Rural and Regional Australia through the TradeStart Program
(Audit Report No. 9, 2005–06)

Helping Carers: the National Respite for Carers Program
(Audit Report No. 58, 2004–05)

Drought Assistance
(Audit Report No. 50, 2004–05)

The Australian Taxation Office's Management of the Energy Grants (Credits) Scheme
(Audit Report No. 20, 2004–05)

ATTACHMENT D: CHECKLIST OF ISSUES TO BE CONSIDERED IN THE DRAFTING OF FUNDING AGREEMENTS

In keeping with Recommendation 16(c), and taking into account considerations of proportionality, an agency developing a funding agreement should examine and address the following issues, to the extent that they are relevant:

- > Name and ABN of the recipient (if applicable).
- > Name and ABN of the funding organisation.
- > Name and year of the funding program.
- > Dollar value of the grant.
- > Time period of the grant and project timing.
- > Amount of funding and schedule of payments.
- > Clauses including compliance with law, employing staff, insurance (public liability) and indemnities.
- > Legal status of the recipient. With the possible exception of small community grants, the agency may require incorporation as a pre-condition of funding.
- > Payments. Payments should be made by instalment in advance or arrears, scheduled in keeping with the achievement of project milestones and linked to performance. There should be a right to withhold and/or recover funding in the event that performance measures are not met satisfactorily or the recipient is in breach of the agreement.
- > Sources of funding. Details of all sources of government funding should be requested from applicants in order to avoid the possibility of applicants 'double dipping' from other Australian Government programs.
- > Co-funding. Consider a requirement that applicants provide information on co-funding of projects to allow the Commonwealth to measure risk of project failure should co-funding fail to eventuate.
- > GST. State whether the grant includes or excludes GST.
- > Money. Consider whether the receipt and expenditure of funds should be separately identified in recipient's accounts. Not likely to be appropriate for small grants for community funding, yet prudent in larger infrastructure grants to facilitate the identity of funds and audit.
- > Interest. Funding to be held in an interest-bearing account and unless otherwise agreed, interest to be used only for the project.
- > Unspent funds. The Commonwealth should have the power to recover unspent funds where those funds have not been legally committed for expenditure or were not spent in accordance with the agreement. The funding agreement may provide for funds to be recoverable as a debt without the requirement of further proof of amount.

- > Assets. Consider the ownership of assets financed by the grant: in particular, whether the agency requires ownership of the asset to revert to the Commonwealth when the agreement expires or is terminated. Consider whether the recipient should pay to the Commonwealth the attributable proportion of proceeds if the funded asset is sold, lost, damaged or disposed of.
- > Intellectual property. Intellectual property created with grant funding is owned by the recipient. Consider whether the agency requires ownership to be transferred, or the licensing of intellectual property to the Commonwealth.
- > Privacy. The grantee must comply with privacy obligations under relevant legislation so as not to expose the Commonwealth to a breach of privacy claim. In addition, the grantee must not breach an Information Privacy Principle.¹⁸⁴ Sub-contracts should include equivalent clauses.
- > Record keeping and inspection of records. Project and financial records must be kept and made available for inspection and/or audit on request.
- > Reporting. Regular reporting on the expenditure of funds and achievement of milestones is required. Insolvency should be notified immediately.
- > Publicity. The recipient may be required to acknowledge the funding provider and/or the Australian Government in publicity about the project.
- > Variations. Consider the manner in which variations may be made: for example, whether any variations must be made in writing.
- > Dispute resolution. Address the procedures to be followed in the event of default or disagreement between the parties.

Agencies should seek legal advice in the drafting and variation of funding agreements.

¹⁸⁴ Information Privacy Principles are the principles set out in section 14 of the *Privacy Act 1988 (Cth)*