

December each year and so would not meet the timeframe set by *Operation Sunlight* and the Senate committee. Bringing reporting forward could be achieved, but this would come at the cost of not using audited financial statement information.

The Auditor-General advises that the unaudited aspect would not be too much of an issue if the main goal was to get the information out early. Final figures could be produced in the CFS.⁴¹ The Auditor General has advised that he is comfortable with the inclusion of audited information in the CFS and considers the provision of unaudited information in a report earlier (say at the end of August) to have limited value.

The 2008–09 Budget papers included a Register of Special Accounts in Budget Paper No 4. The Government has indicated that this Register will be expanded from the 2009–10 Budget to include financial information on Special Accounts. This is a useful advance in accountability. However the Register of Special Accounts contained in Budget Paper No 4 for 2008–09 contains no information other than the name of each Special Account, and the Department administering it, and while Special Account spending is listed in the PBS, it would be useful to have it detailed portfolio-wide as part of the Budget Paper No 4 register.

Recommendation 13: That a consolidated register of Special Accounts be produced, and final audited figures should be produced in the Consolidated Financial Statements.

Net Appropriations

By entering an agreement under Section 31 of the FMA Act, agencies can supplement their Annual Appropriations. Section 31 Agreements are legislative instruments, but are not disallowable. As a result they offer the Parliament no opportunity to provide scrutiny. I have not investigated why these legislative instruments are not disallowable, and that is a matter the JCPAA might like to explore in due course.

ANAO's 2004–05 audit of Net Appropriation agreements, agencies reported Section 31 receipts totalling \$1.46 billion. Those figures contrasted with those for 1996–97, the last full financial year before the commencement of the FMA Act, when Net Appropriation receipts amounted to \$831 million.⁴² This represents an almost 100 per cent increase in an eight year period.

ANAO was interested in how many agreements had been properly executed under the terms of the FMA Act. ANAO found that 68 percent of agreements had been effectively executed, but assessed 18 percent as 'ineffective'. ANAO reported that a number of agencies were unable to provide evidence to demonstrate the effectiveness of the remaining 14 percent.⁴³

The F&PA Committee considered ANAO's audit in its 2007 *Transparency* report. The committee concluded that existing reporting mechanisms in relation to Section 31

41 Department of Finance and Deregulation, *Implementing Operation Sunlight*, p. 13.

42 Australian National Audit Office, *Management of Net Appropriation Agreements*, Audit Report No. 28, 2005–06, p. 14.

43 Australian National Audit Office, *Management of Net Appropriation Agreements*, Audit Report No. 28, 2005–06, p. 19.

Agreements were insufficiently effective.⁴⁴ The evidence led the committee to question whether Section 31 Agreements were the most appropriate vehicles for authorising increases in agencies' Annual Appropriations by the amounts they receive from non-appropriations sources.

The F&PA Committee recommended that the management of Net Appropriations be returned to the Appropriation Acts so as to ensure that these significant transfers of funds are fully transparent to the Parliament, and that if alternative measures were taken, they be reported to Parliament.

The then Government moved to respond to these concerns. As a consequence, the administration of these transactions is set to be revamped at the end of the 2007–08 financial year. New FMA Regulations 15 and 16 replace agreements made under Section 31, which will cease at the introduction of the regulations, by prescribing five broad categories under which funds may be retained by agencies. One of the categories described under the regulations covers amounts taken from Special Accounts. Amounts retained under the regulations must be reported in the relevant PBS, annual report, and from 2009–10, Budget Paper No 4. The level of detail required is unclear.⁴⁵

The substitution of regulations for Section 31 Agreements will remedy the problems in administration. The other underlying issue is the ability of executive government and especially the ability of departmental secretaries and other chief executive officers to use tools such as (but not limited to) these agreements to transfer funds from one form of appropriation to another. The introduction of Agency Resource Statements in Portfolio Budget Statements and Annual Reports from 2008–09 will provide an increased level of information on the amount of Section 31 net appropriations being retained by agencies both at the aggregate level and at the outcome level. The Agency Resource Statements also provide an additional level of transparency of Special Accounts, including details of appropriation receipts, equity injections and non-appropriation receipts.

This together with the inclusion in Budget Paper No 4 of a list of net appropriations from the 2009–10 Budget will provide significantly enhanced information on the use and nature of Section 31. Transfers of administered appropriations between outcomes already require Parliamentary scrutiny, via the need to re-appropriate. As a package these transparency measures will significantly enhance Parliament's ability to scrutinise such transactions.

Recommendation 14: That the Government ensure that transfers of amounts between different forms of appropriation are reported to the Parliament in agencies' financial statements. Reporting should be clear and as explicit as practicable.

Depreciation

The F&PA Committee heard that the provision of appropriations for depreciation of assets is anomalous in that it neglects the fact that at the outset of the new financial arrangements, the Parliament had already provided the funds to acquire the assets being depreciated.

44 Australian National Audit Office, *Management of Net Appropriation Agreements*, Audit Report No. 28, 2005–2006, pp 26, 118 and 121.

45 Draft Finance Circular, *Relevant Agency Receipts – FMA Regulations 15 and 16*, 2008.

Appropriating for depreciation reimburses the agency for appropriations it has already received.⁴⁶

The committee heard that gross capital expenditure should be separately reported and budgeted for as required, with a subdivision of expenditures between asset replacement (i.e., the depreciation component), and asset expansion. This methodology would have the effect of funding depreciation charges each year only as required for replacement purposes in that year. This would avoid the possibility of departments building up internal cash balances for future asset replacement or whatever other purpose they may use to spend the funds on.⁴⁷

Further, the lifespans over which costs are allocated for long life assets may bear little relationship to the real life of the assets, and the annual depreciation charges can be inaccurate in fact. Lifespans are greatly affected by obsolescence, repair and maintenance, and general management of the asset. These matters are not given much consideration in determining asset lifespans for depreciation purposes.⁴⁸ A saving grace is that the accounting standards require lives of assets to be reviewed annually, but that only works if the review process is effective.

Funding for depreciation is opaque and possibly excessive. The Government should also consider new approaches that would result in greater transparency and, in particular, should consider the separate reporting of gross capital expenditure as outlined above. Coupling this approach with proposed revised asset funding arrangements, which centre on implementation of an asset management framework, improved cash forecasting by agencies, and adaptation of the income statement to reflect the net cost of services, appear to be a common-sense way forward. Implementation of such arrangements from 2009–10 should be strongly encouraged.

Recommendation 15: That the Government seek advice from the Department of Finance and Deregulation and the Australian National Audit Office in relation to the treatment of depreciation over the next year, with a view to implementing a new model from 2009–10, addressing weaknesses in the current system.

Annual departmental carryover surpluses

Changes to the financial framework in the 1999–2000 Budget ensured that the annual Appropriation Acts do not lapse at the end of the year, with the result that funds may be carried over from year to year. The amount carried over in 2004–05 was more than \$14 billion, comprising \$7.71 billion in Annual Appropriations, \$5.35 billion in Special Accounts, and \$974 million in limited Special Appropriations.⁴⁹ In addition there are routinely large sums of money that have been appropriated by way of Special Appropriations that are 'carried over' because the appropriation is open ended.

46 Senate Finance and Public Administration Committee, *Transparency and Accountability of Commonwealth Public Funding and Expenditure*, March 2007, p. 57.

47 Senate Finance and Public Administration Committee, *Transparency and Accountability of Commonwealth Public Funding and Expenditure*, March 2007, p. 57.

48 Senate Finance and Public Administration Committee, *Transparency and Accountability of Commonwealth Public Funding and Expenditure*, March 2007, p. 57.

49 Senate Finance and Public Administration Committee, *Transparency and Accountability of Commonwealth Public Funding and Expenditure*, March 2007, p. 27.

Special Appropriations that are limited by amount do carry over from year to year, but only for the purpose within the legislation and only until the limit is reached.

The F&PA Committee canvassed a scenario in which the Executive might make use of carryovers to thwart the will of the Parliament. Through the Executive creating external pools of funding, the ability to withdraw supply could effectively be denied to the Parliament. While it could be argued that the realisation of such a scenario would require extremely large sums to be carried over, the carry-over of \$14 billion in 2004–05 was not unusual, and is not an insignificant sum.

The proposition was put by the committee to the Auditor-General, who responded that:

I think at a conceptual or theoretical level there is something in that. But it is not forever; it is, I imagine, for a relatively constrained period of time because the government needs authority across a very broad range of programs. Whether this level of authority, despite the size of it, provides the breadth and the coverage to allow a government to continue for too long would need deeper analysis. But I think it certainly—put it this way—gives greater authority than there used to exist under a cash system, where the authority lapsed at 30 June.⁵⁰

Any funds carried over at the end of a financial year have at one time or another been legally appropriated, and it might be argued that the ability of agencies to retain funds for future liabilities is conducive to better resource management. However, any perceived increases in managerial efficiency must be considered in the context of loss of parliamentary control of the appropriations.

The F&PA Committee concluded that agencies should report to Finance soon after the end of each financial year the amount of their unexpended funds on each of their outcomes (or programs) and the reasons for the underspend. The Government would then arrange for a consolidated report to be tabled in Parliament within six months. Parliamentarians and the public would thus be informed of any significant underspending on the specific purposes for which funds had been appropriated. The underspent appropriations should be returned to Consolidated Revenue unless the Finance Minister determines that there is good cause why they should be retained by the agency.⁵¹ In the case of parliamentary departments, the Presiding Officers should substitute for the Finance Minister so as to ensure parliamentary independence.

From 2008–09, appropriations for administered expenses will be subject to an annual process by which amounts which are not required to fund activities in the year are extinguished. Agencies' financial statements, as published in their annual reports, will indicate the amounts to be extinguished, ensuring that amounts not required for the year will be returned to the CRF. If Government then wishes to spend that amount in a later financial year, it must seek a further appropriation in a later appropriation bill.⁵²

50 Senate Finance and Public Administration Committee, *Transparency and Accountability of Commonwealth Public Funding and Expenditure*, March 2007, p. 29.

51 Senate Finance and Public Administration Committee, *Transparency and Accountability of Commonwealth Public Funding and Expenditure*, March 2007, p. 30.

52 Commonwealth of Australia, *Budget Agency Resourcing*, Budget Paper No 4, 2008–09, May 2008, p. 8.

The Government is to be congratulated for the introduction of this new process as it will increase budgetary transparency and the Parliament's ability to scrutinise Government expenditure.

It will be important that this change be supported by measures that manage the cost and risk to the Commonwealth agencies accelerating expenditure so as to spend appropriated funds. For example, it would be possible to reinforce existing general obligations and guidance that payments should not be made by the Commonwealth in advance of need. In addition, just as there is a specific obligation in the FMA Act on agencies to bank funds received in a timely manner, there may be benefit in considering the adoption of an explicit requirement governing the timing of payments.

The arrangements for departmental and non-operational funds remain unchanged, whereby a request is made in writing from a responsible minister, the Finance Minister may issue a determination to continue or reduce the entity's departmental expense or non-operating costs appropriation.

If the government ceases appropriating for depreciation the size of departmental appropriations that would carry over to the following year would be considerably decreased. The introduction of the Agency Resource Statement in Portfolio Budget Statements and Annual Reports from the 2008–09 reporting cycle requires agencies to report on expensed but unspent funds at the end of a financial year and will be open to Parliamentary and Government scrutiny. These changes will provide significantly more and clearer information to the Parliament and may obviate the need to go as far as the F&PA Committee concluded. Nevertheless, the Government should consider whether, where large accumulated reserves are evident, agencies should be required to report the reasons for such accumulations in their Portfolio Budget Statements and Annual Reports.

If funding of depreciation were to continue then the Government should consider mandatory reporting on unspent departmental reserves in Portfolio Budget Statements and Annual Reports.

The reporting of unspent portion of appropriations is currently done through the appropriation tables in the notes to the financial statements. This information will be supplemented with the introduction of the agency resource statement to Annual Reports, subject to the agreement of the Joint Committee of Public Accounts and Audit, from 2008–09.

The issue of where 'underspends' actually rest requires clarification. A common understanding is that appropriations move from the CRF into agency hands. More accurately, appropriations are not 'handed' to agencies, as appropriations are an authority for the Executive to spend money from the CRF. Agencies also cannot 'return' cash as the cash remains in the Official Public Account until required. In the same way 'underspends' cannot be 'returned' to the CRF because they have not left it. If they are to be returned, what is actually required is that they be extinguished in law.

Recommendation 16: That the Government require agencies to report any accumulated unspent appropriations and with respect to large amounts the reasons for the underspend in their Portfolio Budget Statements and Annual Reports. Furthermore, that unspent appropriations be returned to the Consolidated Revenue Fund (ie extinguished in law) unless the Finance Minister (or relevant Presiding Officer for

the Parliamentary appropriations) determines that there is good cause for the funds to be retained.

Treating GST as a Commonwealth Tax

For the first time since the 1999–2000 statements, the Consolidated Financial Statements released by Minister Tanner on 20 December 2007 have recognised the GST as a Commonwealth tax. This change is in accordance with the ANAO’s opinions, *Operation Sunlight* and recommendation 7 of F&PA’s *Transparency* report.

The Government is to be congratulated for moving swiftly to end this particularly egregious example of manipulating the Commonwealth accounts for no good end.

Urgent and unforeseen expenditure – advances to the Finance Minister

In situations where entities require extra funding for urgent and unforeseen expenditure, Appropriation Bills 1 and 2 typically contain a clause enabling the Finance Minister to provide urgent additional funding. The Advance to the Finance Minister (AFM) provision is limited to a maximum dollar figure in each of the Bills.⁵³ An AFM provision is typically also included in each successive annual Appropriation Bill. Those provisions have the effect of enabling certain amounts issued under the previous Acts to be ignored, thus resetting the maximum amounts that may be issued.

An advance is only issued if it is the last available legal source of funding. The AFM forms a central contingency fund to provide urgent funding to agencies, through the year, where the appropriated funds prove to be insufficient or a new appropriation is required. It is made available only where agencies are able to meet two essential tests:

- The need for funding must be urgent; and
- The need for funding was unforeseen, or has arisen because of erroneous omission or understatement.

Since 1 January 2005, determinations made under these provisions are registered on the Federal Register of Legislative Instruments and are tabled monthly in Parliament together with explanatory statements relating to the determinations. The determinations set down the purpose of the Advance, the agency receiving the funds, and the amount and the outcome against which the funding is appropriated. Additional information may be found in the explanatory statement, including how the determination meets the tests outlined in the legislation. This was a useful improvement in accountability.

Funds from the AFM may be advanced pending the passage of the Additional Estimates or may remain as a Final Charge for the financial year. Funds provided pending the Additional Estimates may be recovered from agencies when the additional Appropriation Bills are passed. Determinations that are made as a Final Charge are not recovered from agencies during the year. Until recently, those issues were documented in an annual report to

53 The 2007–08 Budget provided for \$175 million and \$215 million in Appropriation Bills 1 and 2, respectively.

Parliament, *Advance to the Finance Minister as a Final Charge*. According to Budget Paper No 4, the reporting to Parliament about the use of the AFM has been changed for the 2008–09 financial year by replacing the *AFM as a Final Charge* with an annual report to Parliament on use of the AFM provision.⁵⁴ The AFM annual report will cover all amounts issued.

The *Advance to the Finance Minister as a Final Charge* has been referred each year with the particulars of proposed expenditure to the relevant Senate (Estimates) committee for inquiry and report. After the Senate votes on the third reading of the additional appropriation bills, the issues document is considered in the Committee of the Whole. It is unclear from Budget Paper No 4 whether this practice will continue with the AFM annual report, but in my view it should.

Another change implemented in the 2008–09 Budget is an increase to the maximum limit of the advance. Appropriations for the AFM have not increased for several years and are now much less significant as a source of funds than in the past. This may be because the additional financial flexibility provided to Government agencies by the outcomes/output framework and especially the ability of agencies to carry over surpluses has alleviated their need to access the AFM. However, the 2008–09 Budget has increased the maximum limit of the AFM provision in Appropriation Bill (No. 1) 2008 to \$295 million and in Appropriation Bill (No. 2) 2008 to \$380 million. The increase was because the previous arrangement for ‘recovering’ AFM amounts from later Appropriation Acts has been discontinued.⁵⁵

At this stage it is unclear whether these changes will result in improved transparency.

While the ability to make highly discretionary appropriations is not ideal from an accountability perspective, provision of a contingency fund for unforeseen occasions and administrative oversight is necessary. This is especially so in an era of relatively ‘big’ Government operating an extensive program agenda. When AFM drawings are made, they are reported to Parliament and subject to examination. Provided rigorous scrutiny takes place, and the quantum of AFM appropriations continues to remain stable, the current system enabling the Finance Minister to make *ad hoc* advances appears sound from an accountability perspective.

Foreseen but not appropriated – the contingency reserve

I would suggest that many would be confused by the existence of what appears to be two contingency measures, the AFMs and the Contingency Reserve (CR). One way to summarise the distinction is that AFMs are unforeseen, while the CR is foreseen but is too general to be appropriated.

Should an item included in the CR in the Budget Papers need access to funds it would then later be provided with these funds through an appropriation bill.

The provisions covering the CR are less rigorous than those governing AFMs, but that is because the CR is not a reserve in the normal accounting sense. In theory it may be possible

54 Commonwealth of Australia, *Budget Agency Resourcing*, Budget Paper No. 4, 2008–09, May 2008, p. 8.

55 Commonwealth of Australia, *Budget Agency Resourcing*, Budget Paper No. 4, 2008–09, May 2008, p. 8.

to put both measures under an AFM process and banner, for greater accountability rigour, and have just one item heading to avoid confusing nomenclature.

I have no settled view but Government and Parliament may consider the broader contingency issue worthy of review.

The CR reflects anticipated events that cannot be assigned to individual programs in the Budget forward estimates. It is not a general policy reserve.⁵⁶ The CR is a global reserve which is supposed to allow for: amounts not yet allocated to individual programs; the tendency to underestimate costs of existing programs in future years; and the tendency to overestimate administered item expenses in the early years as programs get up to speed. This has been called the conservative bias allowance.

Following a review by Treasury and Finance, the conservative bias allowance was reduced in the 2007–08 Mid-year Economic and Fiscal Outlook (MYEFO) to 0.5 per cent of expenses in 2007–08, 1.25 per cent in 2008–09 and 2 per cent in 2009–10. This compared to 0.5 per cent in the first forward year, 1.5 per cent in the second forward year and 2.5 per cent in the third forward year at the previous MYEFO. Notwithstanding the reduced allowance, the current forward estimate for the CR in 2010–11 is approximately \$11 billion.⁵⁷

Operation Sunlight observes that in the lead-up to elections, these unspecified estimates can be important, and that there are no details included on fluctuations between years.⁵⁸ Strictly speaking these are not estimates of appropriations but allowances that still have to be appropriated.⁵⁹ *Operation Sunlight* commits the Government to include in the Budget and the MYEFO a reconciliation table by sub function for changes across the forward estimates. The F&PA Committee supported this approach.⁶⁰

Finance made the point that, while production of such a table is feasible, the extent of disclosure made in the report would need further discussion because the CR is often used to recognise the potential costs for matters that are commercial-in-confidence or national security-in-confidence.

Notwithstanding omissions in detail that might be required to protect matters of commerciality or national security, the production of a reconciliation table would be useful, and would add to transparency. The document should be as detailed as possible in relation to matters that are not sensitive. The recent changes which raise the rate at which reserves are held in forward years make effective disclosure all the more important. Finance should expedite the necessary discussions with the Government so that effective reporting on the CR can commence as soon as practicable.

56 Commonwealth of Australia, Budget Paper No 1, 2008–09 Statement 6: Expenses and Net Capital Investment p. 6–46.

57 Table 21, MYEFO, October 2007, p. 50.

58 *Operation Sunlight*, p. 10.

59 'While the reserve ensures that aggregate estimates are as close as possible to expected outcomes, it is not appropriated. Allowances that are included in the reserve can only be drawn upon once they have been appropriated by Parliament.' Budget Paper No 1 2008–09 Statement 6: Expenses and Net Capital Investment, pp 6–46.

60 Senate Finance and Public Administration Committee, *Transparency and Accountability of Commonwealth Public Funding and Expenditure*, March 2007, p. 60.

I would expect that in the normal cycle of performance reports that the ANAO will review the efficacy of the AFM and of the CR.

Recommendation 17: That the Government include in the Budget Papers a reconciliation table for the Contingency Reserve, containing as great a level of detail as is practical for each item of expenditure.

Recommendation 18: That the Minister for Finance issue public advice on the nature and usage of AFMs and the Contingency Reserve. That in due course the Australian National Audit Office review the efficacy of the AFM and the Contingency Reserve.

The contingency reserve and the war-making power

The CR makes allowance for 'national security-in-confidence items that cannot be disclosed separately'.⁶¹ The CR quite properly deals with national security emergencies that need to be funded as they arise. That proper concern should not lead to loose or late financial authorisation. Governments need access to funds in order to respond to major emergencies and urgent international obligations, but where does the Parliament's role of approving the use of funds fit within these circumstances?

There would be advantages in removing any ambiguity over the use of funds that have not been approved by Parliament for the purposes of meeting Australia's obligations in relation to combat operations, national and international emergencies, and other events requiring Australian Government intervention.

As a basic principle, approval of funds for these activities should be the result of the normal appropriations process. That is not always possible. There are valid circumstances (such as the 2007 cyclone damage in North Queensland) when funds were urgently needed, for which there was no explicit authority from Parliament for the use of funds, and appropriation was subsequently authorised as early as practicable.

Parliament has an appropriate role in the scrutiny of the how these funds are used and in considering the supply of additional funds for these purposes. Like Government, Parliament would, however, want this scrutiny to support the effective use of public funds without hindering the release of funds to meet emergency circumstances.

The fact that full reporting of the CR may be inhibited by national security considerations is no doubt partly based on the potential use of the CR for sudden and unforeseen commitments of the Defence Force.

Under current arrangements the Executive Government, in effect the Prime Minister advising the Governor-General, has the exclusive power to commit the Defence Force to actions potentially involving war-like situations, including interventions in foreign countries. The gap in accountability resulting from this arrangement has been remarked upon in the past, and there have been and are proposals to subject this war-making power to parliamentary control by legislation. That is not the province of this Report, but accountability is.

61 Commonwealth of Australia, Budget Paper No 1 2008–09, Statement 6: Expenses and Net Capital Investment pp 6–46.

The gap in parliamentary control of expenditure which accompanies the gap in accountability outlined above has been less remarked upon. In exercising this war-making power, the executive government may be irrevocably committing the country to high ongoing expenditure over the longer term without parliamentary approval of that expenditure, except retrospective and delayed approval. For instance, the decision of the previous Prime Minister to commit the country to the war in Iraq has cost taxpayers over \$2 billion to date, with the Parliament advised the decision had been made and then subsequently presented with the bill in instalments, for expenditure already made or committed to.

There is a distinction between being invaded, which requires an immediate executive response, and invoking war-like powers externally. From a Budget point of view, it would be preferable if the power to commit the Defence Force to warlike action were subjected to advance parliamentary approval. This would subject potentially very significant government expenditure to early parliamentary scrutiny and control.

This is a larger problem than simply reporting on the CR. Accountability of the CR with respect to national security items, and the problem of firm commitments to war-like expenditure, without or in advance of parliamentary appropriation, indicate a gap in the normal executive responsibility to the Parliament.

Recommendation 19: That the Government report to Parliament on possible mechanisms to bring about enhanced Parliamentary scrutiny of expenditure in circumstances involving responses to domestic and international emergencies, in particular circumstances of war-like action.

Tax expenditures

Treasury defines a tax expenditure as a tax concession that provides a benefit to a specified activity or class of taxpayer. A tax expenditure can be provided in many forms, including a tax exemption, tax deduction, tax offset, concessional tax rate or deferral of a tax liability'.⁶²

Tax expenditures provide what is in effect a subsidy through income foregone for certain activities or categories of persons. The F&PA Committee observed subsidies generally are provided by means of Special Appropriations and the Committee considered that the reporting of tax expenditures should be no less transparent than the reporting of Special Appropriations.⁶³

Tax expenditure is contained in the Tax Expenditures Statement (TES), produced by Treasury each December. The TES is tabled in the Senate, usually on the first sitting day of the following calendar year and under a Procedural Order of the Senate is now formally referred to the legislative and general purpose committees (as a result of my submission on this matter some years ago) for consideration during their examination of the additional estimates.

62 Department of the Treasury, *2006 Tax Expenditures Statement*, December 2006, p. 1.

63 Senate Finance and Public Administration Committee, *Transparency and Accountability of Commonwealth Public Funding and Expenditure*, March 2007, p. 33.

Treasury has observed that concessional arrangements that give rise to tax expenditures often only receive consideration from Parliament at the time they are introduced, and that the cost of tax expenditures is generally not directly observable as it does not arise from a direct transaction with Government.⁶⁴

Treasury have estimated that tax expenditures in 2006–07 will amount to approximately \$41 billion, for those 60 per cent of tax expenditures where an estimate was quantified. General estimates exist that would allow qualified reporting of a further \$15 billion in tax expenditures.⁶⁵ Further understatement exists because the methodologies used do not capture the full cost of the tax expenditures. Even excluding the additional amount identified by ANAO, and the other factors leading to understatement, the quantum of reported tax expenditures is comparable to the amount of expenditure under the largest of the Government's outlay programs, such as the entire estimated spending on Defence for 2008–09.⁶⁶ It is important to keep in mind that tax expenditures incur an opportunity cost. They represent revenue that, if collected, would have been available to fund spending programs (or outlays) to meet similar objectives or to increase the Budget surplus, or to reduce any deficit.⁶⁷

Of particular note over recent years has been the significant under-estimation by departments of tax expenditures, which have been growing markedly. As Dr Mark Burton submits:

On Treasury's figuring the tax expenditure program will cost \$51.4 billion...for the 2007-2008 financial year...this represents a significant increase in the projected tax expenditures from the preceding TES, where tax expenditures for 2007-2008 were projected to be \$46.7 billion.⁶⁸

While the TES may meet the relevant rules for reporting tax expenditures it does not contain any critical commentary regarding the operation of the identified tax expenditures.⁶⁹ The ANAO Performance Audit, tabled in May 2008, found that tax expenditure standards applied by the CBH have not been developed to account explicitly for identifying and estimating the costs of tax expenditures. Nor, the audit found, has there been any significant progress toward regularly evaluating tax expenditures against their objectives or integration of their consideration into the Budget process.⁷⁰

During its 2007 inquiry, the F&PA Committee heard a number of suggestions for greater transparency for reporting tax expenditures. They include:

64 Department of the Treasury, *2005 Tax Expenditures Statement*, December 2005, p. 2.

65 2007–08 MYEFO, Part 4, Attachment D. Australian National Audit Office, *Preparation of the Tax Expenditures Statement*, Audit Report 32, 2007–08, p.19.

66 Commonwealth of Australia, Budget Paper No. 4, 2008–09, p. 35.

67 Australian National Audit Office, *Preparation of the Tax Expenditures Statement*, Audit Report 32, 2007–08, p. 10.

68 Correspondence, Dr Mark Burton, 20 April 2008. In fact, Dr Burton submits that the under-estimation is even greater because of changes to accounting practices between 2006 and 2007.

69 Senate Finance and Public Administration Committee, *Transparency and Accountability of Commonwealth Public Funding and Expenditure*, March 2007, p. 32.

70 Australian National Audit Office, *Preparation of the Tax Expenditures Statement*, Audit Report 32, 2007–08, p. 16.

- Provision of a clear statement of the benchmark taxation principles against which 'tax expenditures' might be ascertained and quantified.
- Identification of all tax expenditures, including reporting on goods and services tax expenditures and matters such as tax evasion, and Commissioner of Taxation lenience for classes of taxpayers.
- Gathering sufficient 'raw' data as to enable informed critical assessment of the operation of tax expenditure, such as the number and characteristics of taxpayers who benefit; the deadweight tax compliance associated with a particular measure; and the use to which the benefit of the tax expenditure is put.
- Publication of a critical appraisal of the merits of each case which explains why the particular tax expenditure has been adopted and also why the tax expenditure has assumed the legislated form.
- The preparation of the tax expenditures report to be undertaken by an independent agency.⁷¹
- Inclusion of detailed tax expenditure in the budget papers, preferably broken down by function in the same way as other expenditure⁷²

Treasury submitted to the committee that inclusion of tax expenditures in the Budget Papers would result in the TES being of diminished use, as it would not be available to provide timely input to Budget planning. The committee found this argument well made, and declined to recommend changing the timing of the TES.⁷³

The Auditor-General's May 2008 performance audit noted that many reviews of tax expenditure have identified problems over the years, and that many solutions, such as those listed above, have been implemented poorly or not at all. The Audit Report concluded that, *inter alia*:

...ongoing review of tax expenditures would be beneficial given the lack of regular, risk-based reviews and evaluations of tax expenditures as to whether they are achieving their objectives and, if so, at what cost. Such a review, and ongoing scrutiny of tax expenditures, would benefit from

- the development of standards to govern the integrated reporting of delays and tax expenditures under the Charter of Budget Honesty...
- the identification of opportunities to better integrate the consideration of outlays and tax expenditures into the annual Budget process, so that the cost of any new tax concessions, and any potential offsetting savings, is fully considered...⁷⁴

I endorse the need for a broad review of tax expenditures, and foresee the benefit to be derived from ongoing scrutiny. However, I am mindful of concerns raised by Dr Mark Burton

71 Senate Finance and Public Administration Committee, *Transparency and Accountability of Commonwealth Public Funding and Expenditure*, March 2007, p. 32.

72 Senate Finance and Public Administration Committee, *Transparency and Accountability of Commonwealth Public Funding and Expenditure*, March 2007, p. 32.

73 Senate Finance and Public Administration Committee, *Transparency and Accountability of Commonwealth Public Funding and Expenditure*, March 2007, pp 32–33.

74 Australian National Audit Office, *Preparation of the Tax Expenditures Statement*, Audit Report 32, 2007–08, pp 13–14.

about inadequate reporting of tax expenditure arrangements sitting outside the Treasury portfolio.⁷⁵ Treasury should ensure that it liaises closely with other portfolios that administer tax expenditures to promote the careful collection of accurate information, which will be a precursor to the success of both the review and ongoing scrutiny.

Recommendation 1 made by the ANAO was that Treasury develop a prioritised review of each existing tax expenditure and publish the outcome of each such tax expenditure review. The ANAO report does not elaborate upon what a tax expenditure review should entail.

Treasury responded by agreeing that such systematic review of tax expenditures is appropriate, but suggested that publication of each such review was a matter for the Minister. This of course is a proper response – the Secretary to the Treasury is not an independent Statutory Officer so Treasury cannot make recommendations independent of the Treasurer.

The question is whether the Parliament should leave this matter to the discretion of the Minister. The publication of tax expenditure reviews should not be a matter for the Minister's discretion. If the annual budget is to contain a transparent reporting of budget measures and their objectives, reference to published tax expenditure reviews not only should be but is mandatory.⁷⁶

Publication of tax expenditure reviews would ensure that the reviews entailed a credible critical appraisal of the costs and benefits associated with each tax expenditure (ie akin to the regulation impact statement process which applies to non-tax legislation).

Indirect outlays (tax expenditures) have a long way to go before they catch up to the accounting and reporting standards that apply to direct outlays. This is particularly so with respect to the need for a settled nationally applicable and comprehensive reporting framework for tax expenditures, a set of benchmarks, and accounting standards. A framework for a comprehensive reporting of Australian tax expenditures needs to be developed. Although the ANAO report takes some steps down this road with its Recommendation 4, there is some way to travel.

Unfortunately, the ANAO recommendation is not strong enough in that it merely recommends that Treasury promote more comprehensive reporting by identifying entities outside the Treasury portfolio that administer tax expenditures and identifying arrangements for obtaining relevant data from those entities.

At paragraph 9 of the ANAO report it is noted that:

Treasury's view is that the best focus for controlling tax expenditures is at the policy development stage by ensuring that the Budget processes require that the cost of any new tax concession proposal (and any savings offsets) are examined in the same way as occurs for outlays.⁷⁷

75 Dr Mark Burton, correspondence, 30 May 2008, relating to Recommendation 4 of the Australian National Audit Office, *Preparation of the Tax Expenditures Statement*, Audit Report 32, 2007–08.

76 Dr Mark Burton, correspondence, 30 May 2008, relating to Recommendation 4 of the Australian National Audit Office, *Preparation of the Tax Expenditures Statement*, Audit Report 32, 2007–08.

77 Australian National Audit Office, *Preparation of the Tax Expenditures Statement*, Audit Report 32, 2007–08, p. 12.

I agree with this view – it is far better that tax legislation be developed with relevant information available. Unfortunately, there is no assurance that relevant information will be available. The ATO is reported to have observed:

For many policy decisions the ATO is asked by the Treasury to assess the likely revenue, departmental and compliance cost impacts of new policy proposals, including tax expenditures. However, data collection that would allow reliable measurement of new tax expenditures is not normally the highest priority. Minimising taxpayer compliance costs and the ATO's departmental costs typically govern the design of administrative arrangements. Accordingly, the ATO has no objections to this recommendation subject to the competing need to minimize the compliance cost burden on taxpayers.⁷⁸

While minimizing taxpayer compliance costs is essential, there is a need to establish whether the provision of particular information might generate managerial benefits for taxpayers and also the ATO. For example, such managerial benefits might arise because the taxpayer has better information available to inform commercial decisions.

Another matter deserving particular attention is the failure to synthesise the tax expenditures operating at Commonwealth and state levels. Tax expenditures should be calculated using common methods so that reporting is accurate and comprehensive. Consistent with recommendation 3 in the ANAO audit, standards should be developed by Treasury, in consultation with relevant parties, and applied nationally upon arrival at a common approach.

Compared to outlays, existing tax expenditures are subject to a less comprehensive management and reporting framework. This hampers the effective monitoring and scrutiny of individual tax expenditures. In many cases, it is not possible to show whether objectives are being achieved and whether the actual benefits are proportionate to the costs.⁷⁹

Operation Sunlight commits the Government to undertake an independent audit and assess existing concessions, as well as produce more detailed outcomes to be achieved through tax expenditures, set in place processes for their periodic review and notionally allocate such expenditures to functions and sub functions to facilitate comparison with other expenditures.⁸⁰ In light of the findings of the F&PA Committee and the ANAO, such a move is sensible and likely to be fruitful.

I do not underestimate the difficulties facing any government seeking to significantly lift the standard of reporting on tax expenditures. Nevertheless, the Government should apply a similar vigour and focus to lifting accountability and reporting standards on tax expenditures that it has applied to direct outlays. At the very least the ANAO recommendations should be advanced.

Recommendation 20: That the recommendations of the Australian National Audit Office May 2008 *Preparation of the Tax Expenditures Statement* Performance Audit be

78 Australian National Audit Office, *Preparation of the Tax Expenditures Statement*, Audit Report 32, 2007–08, p. 77.

79 Australian National Audit Office, *Preparation of the Tax Expenditures Statement*, Audit Report 32, 2007–08, p. 14.

80 *Operation Sunlight*, p. 7.

adopted and implemented by Government, then applied nationally through COAG agreement.⁸¹

Continuous disclosure and reporting

Currently there is no requirement for the continuous disclosure of important financial information. *Operation Sunlight* identifies the problem associated with the inability to report material budgetary changes when they occur:

Stable economic policy is not served by sudden jumps in revenue or expenses throwing out the Budget bottom line between key economic statements. This is made worse when markets and commentators are caught out by the size of the fluctuations. The private sector operates under rules of continuous disclosure. Why shouldn't the public sector?⁸²

One of the key principles of continuous disclosure is the expedited and timely release of relevant or material information. Whilst emphasis has rested in the public sector with the production of substantial reports including the annual report, by the time such reports are released, much of the information contained in the financial statements is significantly dated. In addition, material estimations are often 'hidden' as parameter variations which disguise the real impact of policy decisions and there is no continuous fiscal disclosure to inform users of material variations.

Another principle of continuous disclosure in the private sector is ensuring a properly informed market. A rationale behind the mandatory continuous disclosure regime is that entities will not always have incentives to voluntarily disclose price sensitive information to investors. In the public sector, there is a lack of consistent reporting when expenditure slips and readjustments or 'rephrasing' of forward estimates take place. Such practices can provide opportunities for ministers to announce spending and then re-announce the same spending.

What is required to meet the demands of continuous disclosure and ensure the timely release of substantive information is the availability of up-to-date financial information. The private sector operates under the rules of continuous disclosure as a means to enhance confidence and informed participation by investors in secondary securities markets. Sudden jumps in public sector revenue or expenditure dislocates the Budget bottom line between key economic statements and can catch markets and commentators unawares particularly when fluctuations are sizeable.

In seeking to provide for continuous disclosure as part of *Operation Sunlight*, the Government has committed that Treasury and Finance will be required to: 'publish material changes in revenue or expenses on their websites, and produce and publish consolidated and updated fiscal and cash balances on the Treasury and Finance websites every three months.'⁸³

81 The recommendations of the Australian National Audit Office, *Preparation of the Tax Expenditures Statement*, Audit Report 32, 2007–08 are reproduced in Appendix 2.

82 *Operation Sunlight*, p. 6.

83 *Operation Sunlight*, p. 6.

Finance has stated that publishing additional information from the Budget and forward estimate years would be additional work that requires consideration and that it is operating on the assumption that the continuous disclosure proposal is for the current year only.

Recommendation 21: That in accordance with *Operation Sunlight*, material changes in revenue or expenses for the current Budget year should be published on the Finance and Treasury website as well as the consolidated and updated fiscal and cash balances at least three and not more than four times a year. Given possible resource issues, this recommendation should be implemented over a twelve month period with review of the resource implications at the end of that time.

3.3 The Charter of Budget Honesty and the Intergenerational Report

The Charter of Budget Honesty (CBH) Act was a significant step forward in accountability. It is a framework for the conduct and reporting of fiscal policy.⁸⁴ It has two broad purposes. It seeks to improve fiscal policy by requiring policy to be based on principles of sound fiscal management, and requiring the Government to explain and account for its actions. In addition to a Budget Economic and Fiscal Outlook (BEFO) report, the Act obliges the Government to present a number of other reports annually. These include the Mid Year Economic and Fiscal Outlook (MYEFO) report and a Final Budget Outcome (FBO) report.

The CBH Act also requires the production of a Pre-Election Economic and Fiscal Outlook (PEFO) report during the caretaker period preceding an election, and an Intergenerational Report (IGR) every five years.

Mid-Year Economic and Fiscal Outlook

Section 14 of the Act requires the Treasurer to table a MYEFO report by the end of January in each year or within six months after the last Budget, whichever is later. In practice, the MYEFO has been brought down in October or November. The main content requirement is an update of the economic and fiscal outlook, taking account of all decisions affecting expenses and revenues and thus revising Budget aggregates.⁸⁵

Operation Sunlight bemoans the lack of mandated reporting dates for key publications such as the MYEFO.⁸⁶ Tightening the timeframe around reporting would eliminate any opportunity to release documents very early, leaving a long period during which no update would be published. A way to prevent this would be to require, in the case of MYEFO, that the document take account of the June national accounts quarter data, which is released in September. This would result in MYEFO being released during November but not later than 30 November.⁸⁷

84 The discussion of the *Charter of Budget Honesty Act 1998* section draws extensively from *The Commonwealth Budget: process and presentation*, Research Brief no. 7, 2006–07, Richard Webb, Parliamentary Library, Department of Parliamentary Services, January 2007.

85 *Charter of Budget Honesty Act 1998*, s. 16.

86 *Operation Sunlight*, p. 6.

87 Department of Finance and Deregulation, *Implementing Operation Sunlight*, p. 11.

Recommendation 22: That the Government amend section 14 of the *Charter of Budget Honesty Act 1998* to require the inclusion of the June quarter data in the MYEFO and publication in November of each year.

Monthly reporting

The Finance Minister publishes monthly financial statements for the current financial year but for which, as with the MYEFO, there is no mandated reporting date. As a result, the publication date for such statements varies significantly. However, the timely disclosure of current financial information is central to good management and a transparent and accountable financial framework.

Section 54 of the FMA Act requires the Minister for Finance to publish such statements in a form consistent with the Budget Estimates 'as soon as practicable after the end of each month'. Without a specific mandated reporting date for the monthly financial statement, the date of publication has varied significantly. The monthly financial statement for January 2008 was released in April and the statements for November and December 2007 were released in March 2008 when they were already considerably out of date. No large private sector organisation worthy of respect would be so slow.

As part of *Operation Sunlight*, the Government has committed that Treasury and Finance will be required to: 'mandate the regular publication dates for key economic documents including the monthly financial statement.'⁸⁸

Any increase in the frequency of financial updates should be aligned to the release of the key economic indicators which provide the basis for updating the Budget balances in order to maximise the benefit of any increased reporting. In addition, monthly financial reports should compare actuals to a published profile of expected revenue and expenditure or actual revenue and expenditure in the previous year. The current method of comparing actuals to *pro-rata* estimates could be improved but earlier or more regular publication would not realise much gain in transparency without comparisons against profile expenditure.

While Finance recognises that most monthly financial reports (excluding July and August) could be released earlier and on a specified date, there are resource implications with such a proposal and in some instances, pragmatic reasons why current arrangements have allowed for some flexibility.

Recommendation 23: That monthly financial statements be released by a specific date with the statements of July and August subject to flexibility given the work involved in preparing the annual financial statements and the Final Budget Outcome report. The deadline should be aligned to the release of the key economic indicators which inform the Budget balances. Monthly financial reports for the current financial year should compare actuals to a published profile of expected revenue and expenditure or actual revenue and expenditure in the previous year.

88 *Operation Sunlight*, p. 6.

Final Budget Outcome report

Section 18 of the CBH Act requires the Treasurer to table a Final Budget Outcome (FBO) report for each financial year no later than three months after the end of the financial year.

The FBO is divided into several parts, showing the Budget outcome, General Government Sector financial statements, and a comprehensive section that deals with payments to the states and territories, including GST payments and specific purpose payments. Much of the data in the FBO are aggregated, and tables have been prepared on different bases:

- Part 1 on a GFS basis but excluding the GST
- Part 2 on a GFS basis and including the GST, and
- Part 3 prepared on the Australian Accounting Standards basis but excluding the GST.

This presents an obvious impediment to ease of reading and comparison. The rationale behind the decision to produce reports in different formats appears likely to originate with the former Government's decision to treat the GST as a state tax, a situation that the current Government has already reversed in accordance with the *Operation Sunlight* commitment. This should clear the way for the inclusion of GST across the FBO, and along with the harmonisation of accounting standards to AASB 1049, facilitate the combination of parts 1, 2 and 3 into one GST-inclusive statement, prepared to the AASB 1049 standard.

Recommendation 24: That the Government consolidate parts 1, 2 and 3 of the Final Budget Outcome report and provide one statement which includes GST and is prepared in accordance with AASB 1049.

Pre-election economic and fiscal outlook report

The financial position that an incoming government is likely to face is often an election issue. The PEFO is prepared by the Secretaries of the Treasury and the Department of Finance and Deregulation, during the caretaker period that applies after an election is called.

As stated earlier the CBH Act was a useful advance in accountability. One of its significant innovations was the requirement for the production of a PEFO.⁸⁹ The legislative section authorising its production is remarkably short. While the brevity and lack of specificity of section 22 of the CBH Act may allow a useful discretion to the Secretaries of Treasury and Finance, section 22 could be characterised as 'a bit thin' in content, but I have no view as to how it could be enhanced.

The PEFO usually contains information known by ministers. In 2001, the MYEFO and PEFO were published within a day of each other and the two documents were virtually identical. In essence, the PEFO is an update of the information in the annual budget or MYEFO. It is hard to see how this incumbency advantage can be avoided. The fact is that before the caretaker

89 *The Charter of Budget Honesty Act 1998*, Part 7 – Pre-election economic and fiscal outlook report – s22. Public release of pre-election economic and fiscal outlook report: The responsible Secretaries are, jointly, to publicly release a pre-election economic and fiscal outlook report within 10 days of the issue of the writ for a general election.

convention kicks in, key ministers are quite properly kept up-to-date with the latest data. That same data finds its later expression in the PEFO.

I have observed no problem with the PEFO itself, nor is the independence or integrity of the Secretaries that are responsible for its production in question. If there is a problem, it is a perception, fostered by the intensity of the election campaign period, that the PEFO benefits incumbents.

Others may have ideas, but personally I cannot see any way of improving the PEFO process much. The only possibility may be for the Secretaries to examine a way to strengthen the certificate they sign at the time of publishing PEFO. A decade after the introduction of the CBH Act may be an appropriate time to look at strengthening the PEFO.

One other criticism is that the report is not open to third-party expert independent scrutiny after its release. Given that the PEFO must be released as early as practicable during the caretaker period, and given that its release is time critical due to the short period of the election (typically 33 days) I cannot see how that scrutiny could occur.

Scrutiny can and does occur later, and there has been no material criticism of any of the four PEFOs to date (1998, 2001, 2004 and 2007).

The PEFO has succeeded in providing an independent picture of the financial state of play, diminishing the tendency of past election campaigns that were typified by claims and counter-claims about the true state of Commonwealth finances.

Costing of election commitments

Under section 29 of the CBH Act, the Prime Minister may request the Secretaries of the Treasury and the Department of Finance and Deregulation to prepare costings of publicly-announced government policies. Similarly, the Leader of the Opposition may request the Secretaries to cost publicly-announced opposition policies. In the latter case, the request has to be given to the Prime Minister, who may then agree to refer it to the Secretaries. Importantly, the Charter provides for requests to be made during the caretaker period.⁹⁰ In practice, this restricts the Opposition but not the Government, who have access to departmental resources at all times.

The Secretaries are not obliged or authorised to take any action in relation to the request from the Leader of the Opposition, unless the Prime Minister has referred the request to them.⁹¹

A request from either the Prime Minister or the Leader of the Opposition must be in writing, outline fully the policy to be costed, give relevant details, and state the purpose or intent of the policy.

Section 31 of the CBH Act deals with public release and timing. Unlike the PEFO, the legislation has no specific timing provision, providing for the public release of costings ‘as soon as practicable’ after a costing request has been made and before polling day.

90 *Charter of Budget Honesty Act 1998*, ss. 29(1).

91 *Charter of Budget Honesty Act 1998*, ss. 29(4).

Operation Sunlight proposed to amend arrangements relating to the PEFO and the costing of election commitments. It argues that:

Policies of governments and oppositions are not costed fairly under the Charter. The Charter is heavily biased in favour of the government of the day including the release of the pre-election economic and fiscal outcome up to 10 days into the election campaign with no opportunity for independent scrutiny. Access to costing resources for the Opposition only applies during the heat of an election campaign whereas the Government has access year-round.⁹²

It calls for legislation to allow the Government or Opposition to request the Secretaries to the Departments of Treasury and Finance to prepare a costing of any policies within 12 months of the last day for issue of writs for a general election to the end of the caretaker period. Agreed costings would then be released publicly.

Additional costing access will require increased resources. More difficult to resolve are potential conflicts of interest. On the plus side, allowing the Opposition access to Government departments for costings a year out from the election would be good for policymaking and allow the major parties to enter the caretaker period on a more equal footing. On the negative side, potential conflict could arise for the public service if it had to balance two simultaneous requests from the Government and Opposition. As many of the requests for costing outside the caretaker period would be for policies that have not yet been announced, the current approach of receiving requests via the Prime Minister would not be appropriate.

Related to the confidentiality of the costing requests, further conflict for the public service could arise from meeting with the Opposition. Currently, a representative from the Minister's Office is usually present at such meetings. The Opposition is likely to be more open about the policy being costed if a representative from the Minister's Office is not present. Depending on the individuals involved, and the issues at hand, in some cases this might have a potential to compromise the trust or relationship between the Minister and Department.

Therefore there are several challenges in the implementation of the revised arrangements. These relate mainly to Finance and Treasury maintaining appropriate relationships with their ministers while also carrying out confidential work for the Opposition.⁹³ Presumably methods are in place to address this issue during periods in which current arrangements operate, and could be modified or extended appropriately.

While the current system provides for the Opposition to obtain policy costings, at least potentially, it makes no provision for the needs of minor parties to do so. Section 29 of the CBH Act only requires the Secretaries of Treasury and Finance to prepare costings of opposition and government policies.⁹⁴ Minor parties are doubly disadvantaged; their inability to seek costings during elections is exacerbated by the lack of staffing resources with which they typically operate.

92 *Operation Sunlight*, p. 9.

93 Department of Finance and Deregulation, *Implementing Operation Sunlight*, p. 16.

94 *Charter of Budget Honesty Act 1998* s. 29. Requests for costing of election commitments (1) During the caretaker period for a general election: (a) the Prime Minister may request the responsible Secretaries to prepare costings of publicly announced Government policies; and (b) the Leader of the Opposition may, subject to subclause (4), request the responsible Secretaries to prepare costings of publicly announced Opposition policies.

Expanding access to minor parties has resource and practical implications. Because of the resources required, and the tight time-frames involved, it would seem evident that access to this facility could not be extended to the dozens of political parties and hundreds of independent candidates contesting an election. If access needs to be restricted in some way, it could either be by a party needing to have parliamentary representation already, or by size of parliamentary political party, or both. This might also mean that minor parties (non-Liberal and non-Labor in the present circumstances) would need to have a minimum number of members of Parliament to qualify.

The purpose of the existing provision which confers on the Prime Minister a discretion regarding requests from the Opposition for costings is unclear, but presents an obvious potential barrier to fair access. Unless a compelling reason can be put for its retention, it should not form part of the amended Charter.

Legislation to allow the Government or Opposition to request Treasury and Finance to provide costings for policies announced in the 12 months leading to an election would enhance transparency. It would reduce the powerful 'incumbency bias', at least in regard to the obvious need to cost election policies, that currently pervades different aspects of public administration.

Recommendation 25: That the Government implement the changes to access for election costings proposed in *Operation Sunlight*, and investigate options to make provision for reasonable access to these services by minor parties.

Intergenerational reporting

The CBH requires that the Treasurer publicly release an Intergenerational Report (IGR) every five years to assess the long-term sustainability of current government policies over the following 40 years.⁹⁵

The second IGR was published in 2007, and did not include the impact of climate change. Rather, its conclusions are based on tangible historical factors such as demography, participation rates, tax and expenditure, and do not include the intangible variables associated with environmental change.

Operation Sunlight calls for greater consideration of intergenerational issues, on the basis that demographic shifts in coming decades hold serious implications for government finances, as well as for policy more broadly.

The core recommendation of *Operation Sunlight* is that the intergenerational report should be published more frequently than at its current five yearly interval. It also calls for the inclusion of more information and with data disaggregated to the program level. It considers that more economic trends could be managed by extending the forward estimate period for some programs. The two latter policies (inclusion of program level detail and extending the forward estimates period) seem more applicable to forward estimates than the IGR, which is not a document in which program level information would be appropriate. Changing the reporting interval, however, is a different story.

95 *Charter of Budget Honesty Act 1998*, s. 20.

The interval which currently exists between updates might, in the past, have been sensible as the IGR process and structure was evolving. After all, production of lengthy analyses of demographic shifts is neither simple nor inexpensive. However, it seems clear that contemporary society is no tortoise. We are changing our ways, and in historical terms, rather quickly. It is obvious that policymakers need to maintain an accurate grasp of demographic and other trends, and in 2008, provision of a timely set of indicators at least once per parliamentary term represents a worthwhile investment of resources.

It is of interest to note that the International Public Sector Accounting Standards Board is developing a project to look at reporting such as the inter-generational report. Finance and Treasury will be represented in the review, as well as providing input to accounting developments in the normal way.

Recommendation 26: That the Intergenerational Report be produced at least once each parliamentary term (i.e every three years).

Forward estimates

Consistent with the objectives of *Operation Sunlight*, a revitalisation of the CBH would include increased specificity of spending patterns by program, with an emphasis on demographic pressures also reflected in the extension of forward estimates to six years for programs likely to be subject to demographic change. The costing of new programs would be assessed over a 40 year timeframe.

The extension of the forward estimates to six years, for those programs likely to change under demographic pressure, is a step in the right direction, for the same reasons as accurate intergenerational reports are increasingly valuable. Finance made the point that identification of programs that are likely to come under pressure is not necessarily a straightforward exercise.⁹⁶ This task will be made easier by better defining the definition of 'at risk' programs referred to in *Operation Sunlight* and perhaps by introducing the extended reporting gradually over key demographic priority areas (such as the economic and financial challenges brought on by the ageing of the baby boomers) with other policy areas to follow.

Demographic information is already included in submissions to Government to some extent, but further work could be done that could significantly improve the range and quality of information. However this information will need to be selective to avoid new policy proposals being overly long and as a result being of limited value in decision-making.

The difficulty involved with six year estimates is likely to pale in comparison to the task of devising accurate projections of the impact of new programs over a 40 year timeframe. Trends in demography can arise in the short term, but turn out to be long term in their duration, and can be unexpected. The difficulty in anticipating the nature and rate of progress in technology and science over such a long period is formidable. On practical matters, locating and securing the specialist skills to conduct the modelling is another significant hurdle.

96 Department of Finance & Deregulation, *Implementing Operation Sunlight*, p. 16.

In spite of these obstacles, every endeavour should be made to develop effective and accurate means of devising long-term demographic projections. Ironically, in addition to muddying the waters of future projections, developments in technology have done much to advance the field of statistical and demographic analysis.

Nonetheless, accurate assessment of new programs over 40 years is ambitious at this point in time. Perhaps the solution lies in simply mandating the application of trend data to new programs as and when it becomes available and relatively reliable. While this may seem an obvious suggestion, new programs in the past have sometimes ignored well-established demographic and other data in pursuit of other objectives. Informed planning for the future has, on occasion, taken a back seat to practicality.

The application, as a matter of course, of data which is available and reliable to new program proposals can only assist to inform debate and add value to decision-making processes. This could occur through the inclusion of analysis of any relevant trend data in all new program proposals.

Recommendation 27: That the Government consult with key stakeholders, including relevant Parliamentary committees, on the programs across government that would warrant and could be easily adapted to publish forward estimates out to six years.

Recommendation 28 below on the inclusion of demographic analysis for all new programs is somewhat ambitious, depending on the definition of 'new program'. Such projections can be uncertain, and if Recommendation 28 is accepted, relevance would be a criterion, and a sensitivity analysis would be needed.

Recommendation 28: That the Government require in all new policy proposals the inclusion of relevant demographic analysis.

Finance's role in longer term modelling

A number of inter-related questions need to be considered in relation to providing a longer term modelling capability that can be used in supporting government and reporting to Parliament. These include:

- 'off balance sheet' and expenditure impacts beyond the Forward Estimates and their implications for Budget sustainability and provisioning;
- Finance's role in the Inter-Generational Report;
- the *Operation Sunlight* proposal for a regular report on the distribution of health, welfare and education benefits across taxation groups;
- the reporting of regional and rural expenditure in the Budget Papers; and
- the ability of Finance internally and through related external bodies to provide a 'Think Tank' capability for medium to long term modelling of government expenditures and financial pressures.

There are benefits to the Budget process from the provision of an enhanced capability through Finance and the use of expert analysis from specialist analysts and researchers. The ability to inform early budget considerations by providing a strategic framework within which expenditure proposals could be considered is particularly valuable.

Developing an enhanced capability internal to Government through Finance (as opposed to outsourcing expertise) would improve the overall capability of Government to develop and analyse estimates, not only over the medium and longer term, but also in terms of the quality of the Budget and Forward Estimates.

Further analysis of the nature, extent and focus of such a role would be required. Its interaction with existing longer term modelling functions within agencies and Treasury would need to be examined.

The desired outcome would also require clarification. For example, would Finance produce a report every three years on expenditure issues? This could encompass the distribution reporting envisaged in *Operation Sunlight*, Treasury's consideration of revenue measures, and also look at the trends in regional and rural allocation. The resource implications of such an approach are discussed in Chapter 1.

Recommendation 29: That the Government assess its financial data-analysis and modelling capabilities available through the Department of Finance and Deregulation with a view to either having them enhanced in-house or enhanced through outsourcing to an academic body, funded by Government.

Triple bottom-line information in the IGR

Operation Sunlight recognises that the CBH fails to acknowledge emerging trends in the private sector where corporations are increasingly taking account of the longer-term environmental and social costs and benefits of their actions. It states that 'more can be done via integrated triple bottom-line analysis' and commits the Government to 'investigate the utility of a whole-of-government triple-bottom line (economic, environmental and social) chapter in the Intergenerational report.'

The IGR itself recognises the importance of sustaining economic, social and environmental conditions. It states that 'the wellbeing of successive generations requires sustainable economic, social and environmental conditions.'⁹⁷ It goes on to acknowledge that 'the sustainability of economic growth can be undermined by poor use of resources or degradation of the environment.' The same is true for unstable or adverse social conditions. The impacts of climate change are an obvious and significant omission (even given the hesitancy of the previous Government on this issue) from the 2007 report.

Without recognising and accounting for the impacts of the environmental and social costs and benefits, the IGR overlooks influences that are likely to become increasingly important in the overall assessment of wellbeing of the Australian people.

Recommendation 30: That the Government include key environmental and social impacts, such as climate change, in future intergenerational reports and investigate the utility of including a whole-of-government triple-bottom line chapter.

97 Australian Government, *Intergenerational Report 2007*, June 2006, p. 1.

Strengthening the Charter of Budget Honesty

The CBH Act was passed into law in a period of financial management reform which included whole-of-government accrual financial statements being first audited in the 1996–97 financial year; the implementation in 1997 of an accrual-based outcomes and outputs framework to more directly align the Budget process with the annual reporting framework including the first accrual Budget, and full accrual monthly financial statements for material entities from 1999–2000; and the enactment, with effect from 1 January 1998, of the FMA Act, the CAC Act and the *Auditor-General Act 1997* that collectively prescribe the financial management, accountability and audit regime for public sector entities.

More recently, the adoption of Australian Equivalents to International Financial Reporting Standards and the harmonisation of GAAP and GFS improve financial management and the quality of financial information. The AASB released a harmonised standard AASB 1049 (*Financial Reporting of General Government Sectors by Governments*) for the GGS in October 2006; and the (*Whole of Government and General Government Sector Financial Reporting*) in October 2007 to include GFS harmonisation requirements for whole-of-government financial reporting. As a result only one standard, AASB 1049, will apply from the 2008–09 Budget.

The ANAO suggests that the adoption of AASB 1049 provides a significant opportunity to improve the transparency and relevance of financial information provided by Australian Governments. The integration of these two statements may, due to timing issues, require amendment of the CBH.

The CBH could be strengthened to make it mandatory that the Government provide a statement of explanation with the Budget where a departure from the usual accounting standard has occurred. Any departure should be exceptional. The provision of an explanation for departure from the standard would provide a check point for Parliament to examine the reasonableness of any such move.

Ideally, the CBH would require the Government to comply with AASB 1049, in the same way that companies must comply with Australian Accounting Standards. If this is not done, then at the very least, departures should be minimised and fully explained.

This approach would complement improvements to the transparency of Budget documentation and the quality of disclosure of information within the documentation, as is already underway with the redesign of the Portfolio Budget Statements and the Budget Papers for 2008–09, as well as the harmonisation of the GFS and AAS accounting standards and other recommendations contained in this report.

It is a decade since the CBH Act was enacted. A review would be timely.

Recommendation 31: That the Joint Committee on Public Accounts and Audit consider whether they should review and report on ways in which the *Charter of Budget Honesty Act 1998* could be strengthened.

4 The Parliamentary Imperative – Improving parliamentary practices

Chapter 3 and this chapter deal with my second 'big question', which was '*How to better satisfy the parliamentary imperative?*' Chapter 3 covered improving government practices to achieve that end. This chapter concerns itself with improving parliamentary practices to that end.

The central proposition is that Parliament must itself engage in a periodic review of its effectiveness as an agent of accountability and transparency, both operating as a whole, and by the two houses.

It is axiomatic that high staff turnover inflicts higher training costs and lower productivity on an organisation until its employees are brought up to full capacity. It is no different with Parliamentarians. The House of Representatives Chamber Research Office has figures for the average terms of service of members of that House for the recent 41st Parliament of 10.27 years.

The Senate figure, as an average of the terms of service of all senators since 1901 to date, is 11.16 years. Former President Beahan, in a valedictory speech in 1996, made some observations on senators' terms which included some historical perspective.¹

Knowing turnover to be a feature of a Parliament, the two Houses have developed systems to institutionalise or entrench conventions and practices through Standing Orders and a permanent professional House and Senate staff. This Chapter makes recommendations to further entrench parliamentary accountability mechanisms.

Experience tells us that as a group, members of Parliament are likely not to include large numbers who have specialist expertise in finance and accounting matters. In that respect members of Parliament are no different to the general populace. There will always be many members of Parliament who are not skilled in accounting or finance, many who can not easily get across a balance sheet or profit and loss statement; and even those who may have this ability but might be placed in political or portfolio roles where that is not their primary concern.

In spite of the undoubted influence of the executive and the bureaucracy, it is the parliamentarians who largely drive the design and operation of parliamentary practices. It is the parliamentarians who, in the midst of Budget Estimates, are required to understand the myriad financial information with which they are

1 From Senate Hansard, 27 June 1996, p. 2458): Senator Beahan (Western Australia)—I think there is an informal agreement that the retiring senators will now speak in turn and that I will open up for them. I was going to start by washing the Solvol off my hands, but I won't. It is an interesting phenomenon that the length of service of senators is becoming shorter. If you look at the statistics of the last five decades and the average years of service of those senators elected, you will see that from 1941 to 1950 it was 12.4 years; 1951 to 1960, 13.7 years; 1961 to 1970, 11.4 years; 1971 to 1980, 10.7 years; and—get this—1981 to 1990, 6.3 years; and I think it is still going down. So my time of nine years in the Senate, although it seems very short to me, is above average based on recent trends.

presented. That being the case, financial statements and reports need to be as clear and easy to use and understand as possible – the equivalent of the now-established practice of using plain English in legislation that has so improved its understanding.

4.1 Real time analysis

It has been my observation that too much of the analysis or reaction to budgets and their related or consequent documents has been left to the individual initiative or vigilance of parliamentary members, or to set-piece sessions such as Senate Estimates. More real-time reaction is required.

One way to improve this is to ensure that the specialist committees in this area, including but not limited to the Senate Finance and Public Administration Committee (F&PA) and the Joint Committee on Public Accounts and Audit (JCPAA), give the authority to their secretariats to be more reactive. They should be given specific authority to analyse and react to government financial reporting that is relevant to their areas of interest, and in real time, by providing committee members with pertinent briefs. The committees should consult so as to avoid duplication of their work. As has always been the practice, these would be objectively, not politically, designed. Members of those secretariats should obviously include persons with accounting or finance skills.

Many financial documents are tabled. Some of these deserve a standing instruction to secretariats, to produce a brief to their committee members highlighting by exception items of interest from an accountability perspective. This brief might include monthly financial statements, AFMs, the MYEFO, the FBO and perhaps even the Intergenerational Report.

Recommendation 32: That the Joint Committee on Public Accounts and Audit and the Senate Finance and Public Administration Committee examine the merits of enhancing their secretariats' resources and responsibilities so that real-time briefs pertaining to areas of specific interest on relevant finance accountability measures can be produced for committee members.

4.2 Reducing 'red tape'

The current web of governance and transparency systems pertaining to the public sector is a complex one. It has been woven over many years, almost always in an *ad hoc* manner, often having insufficient regard for the strategic role and significance of individual components forming part of the whole. Such arrangements can give rise to confusion on the part of actors in the system, resulting in incomplete and inefficient coverage of the subject.

Regulatory reviews

In this regard the Productivity Commission is currently conducting a series of annual reviews of the regulatory burdens on business. The Productivity Commission's regulation reviews are directed at identifying regulation that is unnecessarily burdensome, complex or redundant, or duplicates regulations in other jurisdictions.

In 2005, the Government announced the appointment of a Taskforce on Reducing Regulatory Burdens on Business and its intention to introduce an annual red tape reduction agenda. This agenda incorporates a systematic review of Australian government regulation to ensure that current stock is efficient and effective and to identify priority areas where regulation needs to be improved, consolidated or removed.

As part of the reviews, the Productivity Commission is responsible for developing a short list of priority areas with options to alleviate regulatory burden and identify reforms to enhance regulatory consistency across jurisdictions. The ongoing five year cycle of annual reviews involves reviewing, in sequence, regulation that impacts mainly on the areas of the primary sector, manufacturing sector and distributive trades; social and economic infrastructure services; business and consumer services; and economy-wide generic regulation and regulation not addressed earlier in the cycle.²

The Council of Australian Governments (COAG) has also been active in examining ways in which unnecessary regulation of the private sector can be removed. In 2008 COAG established a Working Group on Business Regulation and Competition to examine regulation covering environmental assessment and approvals bilateral agreements; payroll tax administration; trade licences; a Health Workforce IGA; national trade measurement; rail safety regulation reform; the consumer policy framework; product safety; trustee companies; mortgage credit and advice; margin lending; and non-deposit taking institutions.

Public sector red tape review

Managing parliamentary workflow and meeting obligations to the Parliament is an essential responsibility of Australian Government agencies. Ministers and the Parliament expect, and are entitled to, a high level of service in their work. As recognised in a recent ANAO Better Practice Guide titled *Agency Management of Parliamentary Workflow*, periodic agency review of business processes in handling parliamentary workflow can assist agencies to highlight lessons learned and identify where improvements could be made for greater efficiency and maximum effectiveness. Equally, there is benefit in the Parliament giving periodic consideration to whether its various requirements remain appropriate.

2 Productivity Commission, *Annual Review of Regulatory Burdens on Business*, Terms of Reference, 28 February 2007 (www.pc.gov.au/study/regulatoryburdens/information/tor) (accessed 24 April 2008).

While the Productivity Commission and COAG red tape reviews focus on the regulatory burden on the private sector, I propose a similar approach be used to review the burden of over-lapping accountability reports and governance systems in the public sector. Ministers and the Parliament often address issues in a portfolio not cross-portfolio environment that can result in measures that are isolated from a perception of effects across government. It is wise to periodically do some thorough housekeeping to establish whether reports, systems or processes are outdated, irrelevant or ineffective.

Governments and bureaucracies may of course leap at the opportunity to rid themselves of requirements whose primary purpose was and is to satisfy Parliament, and are otherwise regarded by them as costly, time consuming or onerous, or as limiting their freedom of action. For these reasons it is unwise to let the Government be in charge of this housekeeping, although obviously they must and should make proposals for periodic reform. It is the task of Parliament itself to periodically conduct a comprehensive review of cross-government accountability devices and measures, to ensure they remain both necessary and relevant to the Parliament.

There is a need for a parliamentary committee to review annual and special reports and legislative requirements as a whole in order to establish whether there is a continuing need for certain existing processes and reporting obligations across the public sector. A review of finance reporting requirements would consider annual and special reports and legislative requirements and establish whether there is a continuing need for existing processes and reporting obligations.

The JCPAA would appear to be the committee most appropriate to fulfil this role, although there may be a need for some form of resource supplementation and/or support.

The JCPAA already approves, on behalf of the Parliament, the Annual Reporting Guidelines. The requirements have been getting broader and are a significant burden on agencies. While the guidelines include some alternatives, such as reporting via agency websites, there is reluctance (based on anecdotal feedback) for agencies to use those alternatives when likely to be questioned within Senate Estimates hearings on those aspects.

A significant number of requirements could be fulfilled through reporting solely on agency websites or better utilisation of other existing documents. For instance there appears some duplication (in process and content) between agency annual reports and the State of the Service report. Information should be periodically tested for value and some requirements could be time limited. An example in this regard is the 'outsourcing' requirements in annual reports which is not only available from AusTender but is no longer the major issue it was. Consideration could also be given to whether information would be most useful when consolidated across government rather than being left to individual agencies to separately disclose.

The JCPAA would have to take a more active filtering role and be active and consistent in weeding out low value requirements. Another valuable role would be to inform the broader Parliament to ensure that mixed messages are not provided to the public service, for example a Senate committee unnecessarily seeking data in a form

different to that agreed with the JCPAA. Of course House, Joint or Senate committees would continue to conduct themselves as they see fit under standing orders, but guiding principles or views from the JCPAA would be of assistance to them.

To assist the JCPAA in these endeavours, it should be able to call on parties and organisations with expertise in considering issues of red tape and streamlining of regulation and reporting obligations. For example, the JCPAA could be assisted in their review of reporting requirements by staff on secondment from agencies such as the Departments of Finance and Deregulation, and should be able to call on the assistance of the Productivity Commission with its longstanding involvement in seeking to improve the operations of government.

Recommendation 33: That the Joint Committee of Public Accounts and Audit conduct a review of all public sector financial reporting requirements directed at identifying those that are unnecessarily burdensome, complex or redundant, or could be produced in a more effective, efficient manner, without diminishing accountability. This review activity should be supported as necessary by specialist expertise from agencies, including the Productivity Commission.

4.3 Reviewing Budget quality

Australia is fortunate in the high standard of its financial administration and reporting, but it is not perfect and can always benefit from updating and review. Continuous improvement should be an in-built attitude, and Finance no doubt feel that is indeed their attitude. However from the parliamentary perspective there is no formal mechanism for the review of Budget quality. The proposition therefore is that a review mechanism be established to comment on the quality of the Budget and where it could be progressed in terms of transparency and comprehensiveness.

If a parliamentary review were to occur shortly after the publication of the Budget, the danger would be the politicisation of the process in the heat of immediate post-Budget analysis. One way to avoid this would be by an informed critique of each Budget by an external independent 'panel of experts' to provide an assessment to Parliament of the quality of the Budget and its related documentation. Such a panel would provide an assessment of whether the Budget is better or worse than the previous Budget in terms of disclosure and clarity, and what needs to be done to improve it. The panel would meet and report to Parliament in the week after the Budget and the week before Estimates commence.

The value of this process is to inform Senate Estimates committees prior to their hearings of a technical and professional opinion on the Budget.

While perhaps an attractive idea at first glance, this does not seem a practical proposition. It is likely to be difficult to bring together a 'panel of experts' in the period envisaged. It is also likely to be difficult for them to be able to delve deeply into the Budget in such a short period, from a technical and professional accounting and finance perspective.

Currently the media and public commentators do have an ability to review the Budget and its quality in the period after the Budget. While much of the initial public commentary is focussed on the headline items contained within the Budget a number of economists, academics and general government experts do provide varying views of the Budget.

Shortly after the Budget, Senate Estimates committees are able to contribute. Senate committees like F&PA have provided useful insights and commentary on Budget quality in their Estimates reports.

In due course the JCPAA also plays a role in examining the Budget. In the past it has provided commentary on the Budget and the financial framework in general. The conduct of ‘roundtable’ discussions on the financial framework has played a significant role in informing the Government and Finance of the views of the Parliament.

Perhaps what is needed is a more precise approach by the JCPAA. The JCPAA could decide to give itself a standing reference to explicitly include examination of the quality of the Budget and related processes in its remit. This could be a formal annual review undertaken post-Budget, enabling a more in depth examination of finance and accounting issues and issues of interest to the Parliament – such as the structure of the Budget Papers and improvements in transparency and useability.

Lastly, the Government itself could furnish the Parliament with a report every three years on the quality of the Budget. The report should examine initiatives to improve quality, transparency and accountability as well as setting out the Government’s agenda for improvement in the next period. This should then be examined by the JCPAA.

There is no reason why the Government should not provide such a triennial report to Parliament, in fact quite the reverse – it would be useful for it to do so.

Recommendation 34: That the Government produce a report on the quality, transparency and readability of Budget documents and information at least every three years, and that it be examined and reported upon by the Joint Committee on Public Accounts and Audit to provide impetus to continuous improvement to Budget transparency and accountability.

4.4 Ministerial accountability between the Houses

Ministers sitting in one House of Parliament cannot be required to appear before committees formed in another. This is most notable in the case of Senate Estimates, when a minister who is a member of the lower house typically appoints a government senator (invariably at least of the rank of a Parliamentary Secretary) to represent their portfolio and take questions from the committee on their behalf.

The delegate senator is rarely able to provide the level of detail in response to committee questions that might reasonably be expected of the minister. Notwithstanding the possibility that detailed responses might be provided at a later date as a result of the question being taken on notice, the diminution in transparency and thus accountability is apparent.

The legal persona of a minister is separate from the legal persona of a member or senator. While I support the convention that members of one House should not be held accountable in another House in their capacity as members of Parliament, membership and representation of the executive is a different proposition. As members of the executive, ministers, if they are in the Senate, should be accountable to House committees in that capacity and ministers in the House of Representatives should be accountable to Senate committees.

Ministers automatically front up to committees in some European parliaments, for instance, through the adoption of mutually agreed procedures between Houses. Ministers may have a much more interactive relationship with committees in some countries because the committees themselves have different functions to Australian parliamentary committees, including ‘clearing’ budgets and writing legislation.

No-one has ever disputed that ministers are accountable to the other House; thus, for example, senators put questions on notice to House of Representatives ministers and the questions are answered. It is not a matter of establishing accountability but of providing a better means of carrying it out.

The appearance of ministers of one House before committees of the other House is simply a matter of cooperative agreement. House of Representatives ministers have often appeared voluntarily before Senate committees.

There is nothing to stop the Australian Parliament agreeing on procedures to bring about a better representation of portfolio ministers, regardless of their House of membership, before properly constituted Parliamentary committees.

Recommendation 35: That the Senate Procedure Committee examine ways of enhancing cooperative arrangements whereby ministers from one House may appear before the committees of the other.

4.5 Ministerial remuneration in the Commonwealth Financial Statements

The ANAO has reported for a number of years that the Commonwealth Financial Statements (CFS) do not disclose the remuneration of ministers.³

For corporate entities, disclosure is currently required for Key Management Personnel, including Directors, by Australian Accounting Standard AASB 124

3 See, for example, ANAO, Audit Reports 15 of 2006–07 and 18 of 2007–08.

Related Party Disclosure. There is currently no equivalent requirement for public sector entities.

There is a range of considerations in determining the manner and form of any such disclosures in a public sector context, including the extent to which information is already publicly available, the extent to which a benefit was personal and the valuation of certain benefits. Given the discretionary nature of the disclosure, and the public sector specific considerations, the details reported could include both quantitative and narrative disclosures.

The ANAO has previously suggested that there would be benefit in exploring whether, as a minimum, an aggregate disclosure of ministerial salaries and allowances could be introduced as is the case in New Zealand.⁴

The Australian Accounting Standards Board intends to consider whether AASB 124, including matters relating to director and executive remuneration, should apply to all not-for-profit public sector reporting entities. An issues paper is planned for later in 2008, and an exposure draft for a standard in 2009.

Recommendation 36: That the Government disclose ministerial remuneration and consider, as an initial step, adopting the New Zealand approach to disclosure of ministerial remuneration, by including an aggregate of the total salaries and allowances provided in the Consolidated Financial Statements.

4 ANAO, Audit Report 18 of 2007–08, p. 40.

5 Good governance

My third 'big question' was *'How to improve governance?'*

In answering this question I set out my approach for this Chapter as follows:

Modern Australian agencies operate under a devolved system of responsibility, whereby ministers and agency executives (and boards in some agencies) are responsible for their own performance, subject to whole-of-government fiscal, strategic and operational determinations.

The report should address parliamentary committee; ANAO; Finance; Labor and other relevant initiatives/suggestions, and suggest ways in which devolution can be better balanced with whole-of-government requirements on the budgetary front.

In particular:

- how (given the absence of an APRA/ASIC type regulator for the public sector), enforcement of key laws, regulations and directions to agencies can be secured across all affected agencies;
- how continuous disclosure and reporting might occur; and
- how policy decisions and their financial implications can be better reported progressively, particularly where the policy is financially open-ended.

Subsequently I decided the continuous disclosure and reporting was better placed in Chapter 3.

Governance relates to the manner in which power is exercised and managed. Governance includes how a government operates, how it is managed, its corporate and other structures, the dictates of its laws, regulations and operating procedures, how it resolves disputes and conflicts of interest, how compliance is secured, and its ethical culture. Good governance is grounded in transparency, accountability, the free flow of information, responsiveness to the needs and aspirations of the people, a commitment to fight corruption, and a professional public service.

I do not intend to tackle such a large topic here. In due course it may be that the Joint Committee of Public Accounts and Audit (JCPAA) might wish to examine governance in the public sector more broadly.

The focus of this chapter is on seeking to improve governance arrangements and the overall level of confidence in the administration of public funds. I do not wish to give the impression that every compliance failure is the result of negligence or bad faith. While non-compliance is of concern, the vast majority of non-compliance events are likely to arise from relatively benign reasons such as poor interpretation of requirements by agency staff, inadequate training, system complexities and workload volume. Even a single wrong or misdirected approach can lead to multiple breaches.

The main message is that there should be a focus on remediation of current deficiencies and improving the standard of financial administration. There is also a

need to acknowledge the primary management responsibility of agency heads under the *Public Service Act 1999* (PS Act) and the *Financial Management and Accountability Act 1997* (FMA Act).

Agency CEOs are responsible for following up non-compliance and imposing remedial action, including discipline, and must retain this role. Rather than a regulator displacing or usurping this role, it is suggested that a regulator should play a proactive but supportive role that emphasises ongoing improvement and the raising of standards across the public sector.

5.1 Enforcement within the public sector

The move to devolution represented a philosophical shift in public sector governance that has subsequently been reinforced by a cultural shift. I remain a supporter of the notion that responsibility and accountability must rest with the agency or entity.

There are those who respond that at its worst devolution in some agencies has resulted in a wilful evasion of central tenets of good public administration and a defiance of whole-of-government policy. That may be true in certain instances, but it does not justify the re-imposition of central control. If a reimposition of central control was desired (and there is no hint there is such a desire), with respect to primary departments like Finance, they probably need to know more of what agencies are doing at the financial management level, rather than necessarily needing to control more.

Transparency and effective reporting is a key way of ensuring devolution is responsibly exercised.

There are significant problems that need to be addressed. Whilst providing a greater degree of flexibility and responsiveness, the devolution of authority and accountability to agency heads, resulting from various public sector reforms over almost two decades, have significantly increased the risk profile of agencies.

The FMA Act, the *Commonwealth Authorities and Companies Act 1997* (CAC Act) and *Auditor-General Act 1997* uphold the Commonwealth's financial framework by providing a legislative framework which emphasises amongst other things, devolved responsibility.

Under the FMA Act and PS Act, agency chief executives are responsible for the management of their agencies including the conduct of employees, compliance with the relevant financial legislation and policy, and the overall ethical performance of the agency. This includes responsibility to 'investigate possible breaches of legislation (and non-compliance with Australian Government policy) by agency employees and to initiate any appropriate remedial and/or disciplinary action.'¹ Indeed, a fundamental

1 Department of Finance and Deregulation, *The financial framework—accountability for compliance and dealing with breaches*, Finance Circular No. 2005–06, p. 1.

aspect of the development of the Commonwealth's current financial framework is performance of public sector responsibilities which inherently include the 'obligation to act legally and ethically.'²

Under the FMA Act, key responsibilities and powers are vested with the Minister for Finance and Deregulation who may delegate to agency heads all those powers other than the power to make 'Finance Minister's Orders.'

In a number of instances enforcement and compliance to ensure that this legislative framework is adhered to has been shown to be weak, as will be illustrated below. The ANAO and others may well uncover breaches or poor compliance in due course, but what is needed is for breaches and non-compliance to be addressed sooner or even in real-time, not years later.

I am of the view that a public service regulator is required.

5.2 Compliance failures

Over the past decade the ANAO and the JCPAA have investigated, and reported on, a long list of compliance failures within the financial framework. The following examples provide an overview of shortcomings in the management of the financial framework in terms of both compliance with financial procedure and demonstrated awareness of the legislation upon which the financial framework is grounded. In demonstrating the inadequacies of the current level of compliance with the financial framework, such examples highlight the need for an independent review process which would ensure that such transgressions are investigated and systematically addressed with a view to strengthening financial management and accountability.

Money spent without appropriation

The ANAO Audit Report No. 28 of 2005–06 examines 231 Section 31 Agreements made between the commencement of the FMA Act on 1 January 1998 and 30 June 2005. The audit concluded that there were widespread shortcomings in the administration of net appropriation arrangements with substantial amounts identified as having been spent without appropriation in contravention of section 83 of the Constitution.³ 'Where the section 83 breach was a result of the agency signatory to an agreement not being authorised or the agency not having an agreement, a corresponding breach of section 48 of the FMA Act was also required to be reported,

2 Kennedy, M. then Assistant Secretary, Accounting Policy Branch, Department of Finance, 1992, cited in Australian National Audit Office, *Management of Net Appropriation Agreements*, Audit Report No. 29, 2005–06, p. 89.

3 The ANAO found 42 agreements across 23 agencies to be 'ineffective' (Australian National Audit Office, *Management of Net Appropriation Agreements*, Audit Report No. 28, 2005–06, p. 23).

given the specific obligations placed on agency chief executives under that section to keep proper accounts and records.⁴

Under section 48, a chief executive must ensure that accounts and records of the agency are kept as required by the Finance Minister's Orders. In addition, section 44 of the FMA Act requires a chief executive to manage the affairs of the agency in a way that promotes efficient, effective and ethical use of the Commonwealth resources for which the chief executive is responsible.

The ANAO identified 14 agencies that had reported their respective annual appropriations to have been increased by receipts totalling \$105.31 million that had not been captured by a Section 31 Agreement. Three of those agencies disclosed \$62.76 million of those receipts as having been spent without appropriation between 1997–98 and 2004–05, in contravention of section 83 of the Constitution and section 48 of the FMA Act.⁵ A further two agencies spent \$1.59 billion prior to having a Section 31 Agreement in place.⁶

There are no criminal penalties for a breach of section 83 of the Constitution. However, there are criminal penalties in relation to a breach of the FMA Act, when a valid drawing right has not been issued. In effect, the relevant provision provides a sanction over the process by which funds are drawn against appropriations, rather than governing whether an appropriation was in place.

The ANAO report raises a number of questions concerning the culpability of chief executives in relation to section 83 breaches. Chief executives are responsible under the FMA Act for the financial management of their respective agency. In addition, where the chief executive is the secretary of a department, or head of an executive agency established under section 66 of the PS Act, the chief executive is responsible for managing the agency, and is accountable to the government, the Parliament and the public.⁷

In its report, the ANAO stated that section 48 of the FMA Act 'imposes a positive duty upon each agency Chief Executive to ensure that appropriations are lawfully available before spending funds. Agency Chief Executives are also responsible for the maintenance of adequate accounting records and internal controls that are designed to prevent and detect fraud and error.'⁸ The ANAO noted that to the extent that agencies made no record of an 'express authorisation provided by their Minister in respect to an official executing a document with significant Constitutional consequences, those

4 Australian National Audit Office, *Management of Net Appropriation Agreements*, Audit Report No. 28, 2005–06, p. 20.

5 Australian National Audit Office, *Management of Net Appropriation Agreements*, Audit Report No. 28, 2005–06, p. 24.

6 Australian National Audit Office, *Management of Net Appropriation Agreements*, Audit Report No. 28, 2005–06, p. 25.

7 *Public Service Act 1990*, s. 66.

8 Australian National Audit Office, *Management of Net Appropriation Agreements*, Audit Report No. 28, 2005–06, p. 133.

agencies have not fulfilled their accountability obligations to the Government and the Parliament.⁹

By the ANAO's standards this is strong language. There is no record of any agency Chief Executive Officer (CEO) or Chief Finance Officer (CFO) suffering any penalty for these 'shortcomings'. That said, these matters are usually discussed between heads of agencies and their minister rather than being matters on the public record.

Special Appropriations

In April 2005, the JCPAA held a public hearing to assess the extent to which agencies had implemented the recommendations of ANAO in its audit, *Financial Management of Special Appropriations*, Report No. 15 of 2004–05.

The issue of administrative penalties was indirectly raised by the committee in so far as it questioned the issue of performance bonuses, stating that whilst many public servants were paid performance bonuses for their financial management skills, they were at the same time, in breach of section 83 of the Constitution or were not appropriately reporting on and/or disclosing significant financial management issues.¹⁰ Whilst urging CFOs to develop a greater understanding of the special appropriations that exist within their specific legislation, the JCPAA recommended that CFO performance bonuses be linked to a demonstrated knowledge of correct procedures for the management and reporting of all relevant special appropriations.¹¹ The Government has yet to respond to the recommendation.

Similarly, in its Report 376, the JCPAA recommended that 'knowledge of, and appropriate use of, financial information be identified in all managers performance agreements.'¹²

The JCPAA noted in its Report 404 some disappointment that the majority of Commonwealth entities audited by the ANAO were not managing and correctly reporting their special appropriations. The committee stated that as special appropriations are part of the legislation for financial management, it was alarmed that it took an ANAO audit to bring to light such discrepancies.¹³

9 Australian National Audit Office, *Management of Net Appropriation Agreements*, Audit Report No. 28, 2005–06, p. 96.

10 Joint Committee of Public Accounts and Audit, Report 404. *Review of Auditor-General's Reports 2003–04 Third & Fourth Quarters; and First and Second Quarters of 2004–05*, October 2005, p. 185.

11 Joint Committee of Public Accounts and Audit, Report 404. *Review of Auditor-General's Reports 2003–04 Third & Fourth Quarters; and First and Second Quarters of 2004–05*, October 2005, Recommendation 34, p. xxv.

12 Joint Committee of Public Accounts and Audit, Report 376, *Review of Auditor-General's Reports 1999–00: First Quarter*, May 2000, Recommendation 1.

13 Joint Committee of Public Accounts and Audit, Report 404. *Review of Auditor-General's Reports 2003–04 Third & Fourth Quarters; and First and Second Quarters of 2004–05*, October 2005, p. 178.

The JCPAA held that a theme that had developed in its review of the financial management of special appropriations and in other reviews of financial management within the public sector (including that on the management of special accounts and investment of public funds), was that managers at senior levels were 'either not fully aware of their responsibilities under the FMA Act, or are not discharging them appropriately.'¹⁴

Again, there is no record of any agency CEO or CFO suffering any penalty for these 'shortcomings'. Again, that said, these matters are usually discussed between heads of agencies and their minister rather than being matters on the public record.

Special Accounts

In its audit of Special Accounts, the ANAO identified widespread mismanagement in terms of non-reporting, non-compliance and deficiencies of special accounts by agencies.¹⁵ The ANAO had found that agencies had not complied with a number of provisions of the FMA Act relating to the management of appropriations, maintenance of proper accounts and records, and the reporting of all special accounts.

In its review of the ANAO audits, the JCPAA held that the centralised supervision provided by Finance was inadequate and may lead to instances of poor administration of special accounts by agencies in the future.¹⁶ The JCPAA recommended that Finance raise the level of agency accountability for their special appropriations by developing appropriate special account management standards to complement the *Finance Guidelines for the Management of Special Accounts* and to which such agencies could report annually.¹⁷ This situation was addressed by Finance in 2006 with the inclusion of a Special Accounts Management Checklist at Attachment D of Finance Circular 2006/08 in relation to the introduction of the Compliance Certificate.

Questions were raised before the Senate Finance and Public Administration Committee (F&PA) in regard to the parliamentary control over special account funds. According to the committee, potentially the 'executive government's ability and especially the ability of departmental secretaries and other chief executive officers to transfer funds from one form of appropriation to another could significantly

14 Joint Committee of Public Accounts and Audit, Report 404, *Review of Auditor-General's Reports 2003–2004 Third & Fourth Quarters; and First and Second Quarters of 2004–2005*, October 2005, p. 191.

15 Australian National Audit Office, *Agency Management of Special Accounts*, Audit Report No. 24, 2003–04, p. 18.

16 Joint Committee of Public Accounts and Audit, Report 402, *Review of Auditor-General's Reports 2003–2004 Third & Fourth Quarters; and First and Second Quarters of 2004–2005*, October 2005, p. 91.

17 Joint Committee of Public Accounts and Audit, Report 402, *Review of Auditor-General's Reports 2003–04: First and Second Quarters*, August 2004, p. 92.

compromise the Parliament's ability to control and scrutinise Government expenditure.¹⁸

In addition, the ANAO raised the issue of the uncertainty as to the 'transfer of amounts within and across the various forms of appropriations, together with the extent of transparency over such transactions'.¹⁹ Whilst such matters raise questions about the clarity of the current system and improving the transparency and compliance of net appropriation transfers, they also provide an opportunity for greater administrative scrutiny by way of independent regulation.

Certificate of Compliance

A number of ANAO financial audits have revealed shortcomings in relation to appropriations and compliance with the requirements of the financial framework. Similarly, the JCPAA has emphasised the importance that Parliament places on compliance with the legislation that establishes the financial framework.²⁰

As a result of all of these concerns greater attention to legislative compliance led to the introduction of the chief executive's annual Certificate of Compliance with specified elements of the financial management framework. Directors of CAC Act authorities and wholly owned companies in the General Government Sector are also required to provide a report on compliance with relevant aspects of CAC Act legislation. Both the certificate and the report are done on a self-assessment basis.

There have been some improvements, with the 2007 Certificate returns revealing that many breaches identified relate to requirements of the FMA or CAC Regulations and Orders rather than the requirements of the legislation itself. That is, in regard to commitment, approval and spending of public funds, failure to document the reasons for non-adherence to the Commonwealth Procurement guidelines and non adherence to time related requirements.²¹

According to the Auditor-General, Finance has indicated that in respect of future audit reports that consider financial framework issues, it will write to the relevant chief executives regarding their responsibilities under the financial framework to investigate compliance failings and suggesting that consideration be given to

18 Senate Finance and Public Administration Committee, *Transparency and accountability of Commonwealth public funding and expenditure*, 2007, p. 22.

19 Australian National Audit Office, *Supplementary Submission 4b* cited in Senate Finance and Public Administration Committee, *Transparency and accountability of Commonwealth public funding and expenditure*, 2007, p. 21.

20 Mr Ian McPhee, Auditor-General, *ANAO's Contribution to Improving Public Sector Administration*, 21 February 2008, p.10.
www.anao.gov.au/uploads/documents/CEF_ANAOs_Improving_PSA.pdf (accessed 18 April 2008).

21 Mr Ian McPhee, Auditor-General, *ANAO's Contribution to Improving Public Sector Administration*, 21 February 2008, p. 11.

informing the responsible minister and/or Parliament of the results of that investigation.²²

In my view, whilst internal investigation and review is necessary, an external, independent process is also required.

Justification for use of public funds

Under the current provisions of the financial framework, approvers of proposals to spend public funds, including ministers, are not required to record the basis on which they were satisfied that a proposal represents an efficient and effective use of public money. FMA Regulation 12 requires approvers of public funds (a minister, chief executive or authorised official) to record the terms of any approval of a spending proposal. However, the Regulations do not specifically require approvers to record the nature and extent of the inquiries they undertake or the basis on which the approver was satisfied that the proposed expenditure would be in accordance with the policies of the Commonwealth and make efficient and effective use of the public money, as required under Regulation 9.²³

In a number of performance audit reports in recent years and particularly in respect to the administration of discretionary grant programs, the ANAO has highlighted the risks to transparency and accountability that arise due to the financial framework not requiring reasons for decisions to be recorded where this is not apparent from the existing documentation (as an adjunct to the existing requirement to record the terms of the decision). ANAO Audit Report No. 14 of 2007–08, *Performance Audit of the Regional Partnership Programme* referred explicitly to this matter.

The ANAO recommends an amendment to the FMA Regulations to require approvers of spending proposals to record the basis for their decision where this is not apparent from the existing documentation.²⁴

In addition, however, the presence of a public sector regulator would further strengthen the transparency of financial decisions, ensuring a supervisory role of such decisions when required, and ensuring that the requirements are met within an effective financial framework.

22 Mr Ian McPhee, Auditor General, *ANAO's Contribution to Improving Public Sector Administration*, 21 February 2008, p. 10.

23 FMA Regulation 9 requires that an approver of a proposal to spend public money must be satisfied that the proposed expenditure is in accordance with the policies of the Commonwealth, will make efficient and effective use of the money and, if the proposal is one to spend special public money, is consistent with the terms under which the money is held.

24 See further, Australian National Audit Office, *Briefing note no. 4. Recording the reasons for decisions to spend public money*, 3 April 2008.

Public interest obligations

The FMA Act and the CAC Act can create real tension between public and individual responsibilities. 'Chief executives confront a situation under the FMA Act where a ministerial direction is considered to be potentially inconsistent with their primary obligation under the Act to manage the agency's affairs and Commonwealth resources in the most efficient, effective and ethical way'.²⁵

Similarly, tensions can arise for Commonwealth agencies under the CAC Act as provisions take into account the 'public interest' obligations which directors and other senior managers have under the Act.²⁶ However, unlike corporate governance legislation in some states, the duties of directors 'are not expressly modified to account for ministerial directions, community service obligations and other public accountability mechanisms'.²⁷

Such tensions could be reported to a public sector regulator with the powers of investigation, adjudication, regulation and enforcement.

Financial delegations for the expenditure of public monies in FMA agencies

In its Audit Report No. 42 of 2003–04, the ANAO concluded that whilst most agencies had developed control structures for the application of financial delegations for the expenditure of public funds which were adequate, financial delegations were not always managed in accordance with the relevant legislation. The ANAO noted that the requirement to document the approval of a spending proposal was not being adhered to in the majority of cases and in some organisations, the statutory power for entering into contracts, agreements and arrangements was incorrectly referenced.²⁸

In addition, the ANAO established that the number of approvals being granted by inappropriate delegates was higher than expected, given that financial delegations are a routine and well established control. However, as noted by the ANAO, it is up to the chief executives to determine the acceptable level of error and to implement controls, guidance and training. Yet, as the ANAO suggested, such controls should be complemented by adequate guidance and training.²⁹ Indeed, for the chief executives

25 Edwards, M. *Public Sector Governance – Future Issues for Australia*, Australian Journal of Public Administration 61(2), June 2002, p. 52.

26 Section 5 of the CAC Act has recently been amended. The amendments define an 'officer' as a 'director or a senior manager of a Commonwealth authority'.

27 Horrigan 2001 cited in Edwards, M. *Public Sector Governance – Future Issues for Australia*, Australian Journal of Public Administration 61(2), p. 53, June 2002.

28 Australian National Audit Office (ANAO), Report 42, *Financial Delegations for the Expenditure of Public Monies in FMA Agencies*, Audit Report No. 42, 2003–04, April 2004, p. 10.

29 Australian National Audit Office, Report 42, *Financial Delegations for the Expenditure of Public Monies in FMA Agencies*, Audit Report No. 42, 2003–04, April 2004, p. 11.

to uphold their accountability and governance obligations in a devolved environment, an 'effective control structure must be designed and maintained'.³⁰

The question remains as to what formal mechanisms currently exist to deal with situations in which the actions of ministers, CEOs and CFOs may result in a failure to adhere to constitutional requirements, Finance Directives and operating procedures. It is worth noting that there is no mechanism, nor is there a requirement, for CEOs to comply with their own Chief Executive Instructions.

Some mechanisms do exist as part of the operations of the Ombudsman, the ANAO, and the Australian Public Service Commission (APSC). Less frequent or occasional alternative avenues such as parliamentary inquiries and royal commissions are also possible, but such mechanisms are sporadic and ad hoc and often occur years later.

There is no single, national process equivalent for the public sector to that instituted in the private sector by the Australian Securities and Investments Commission (ASIC). There is an accountability gap in the existing enforcement mechanisms with existing enforcement agencies not being able to respond most effectively to breaches of the Constitution and the Commonwealth's financial framework and to deter further breaches.

5.3 Existing public sector 'enforcers'

The Commonwealth Ombudsman, the Auditor-General, and the Public Service Commissioner do not have an enforcement role.

The Commonwealth Ombudsman

The Commonwealth Ombudsman has the power to consider and investigate complaints regarding alleged unfair or unreasonable treatment by an Australian Government department or agency.

The Commonwealth Ombudsman can conduct investigations on its own motion, has certain entry and witness examination powers, and can make recommendations to the government but it cannot override the decisions of agencies or issue directions to their staff.

Whilst the Ombudsman can make a formal recommendation to senior management under paragraph 15(3)(b) of the *Commonwealth Ombudsman Act 1976*, there are no additional powers available to the Ombudsman to enforce such recommendations. If adequate action is not taken in response to the Ombudsman's recommendations, the only recourse of the Ombudsman is to report such to the Prime Minister and the Parliament.

30 Australian National Audit Office, Report 42, *Financial Delegations for the Expenditure of Public Monies in FMA Agencies*, Audit Report No. 42, 2003–04, April 2004, p. 19.

In my opinion it would be unwise to alter the powers of the Ombudsman in these respects. The current effective operation of that Office should not be disturbed.

The Auditor-General

The Auditor-General has certain entry and information-gathering powers but it is not an enforcement agency. The Auditor-General has the power to make particular reference to Constitutional and legislative breaches in an ANAO audit opinion on financial statements, and in an ANAO performance audit. However, there are no other mechanisms available for the ANAO to take the issue any further.

For example (as discussed above) in the case of the ANAO Audit No. 28 of 2005–06 concerning the *Management of Net Appropriation Agreements* made under section 31 of the FMA Act, the ANAO found that a number of Section 31 Agreements, upon which agencies relied for an appropriation authority, were invalid. As a result of the invalidity of the agreements, such agencies had no valid appropriation for the expenditure of some amounts (an inadvertent breach of section 83 of the Constitution) and the ANAO found that the accounts and records were not kept as required (a breach of section 48 of the FMA Act).

Whilst breaches of the Constitution are very serious matters, the ANAO's powers only extend to reporting such breaches in its opinion. Therefore, if political intransigence or an inadequate minister result in such matters not being attended to, then necessary remedial action can be stymied.

In my opinion it would be unwise to alter the powers of the ANAO in these respects. The current effective operation of that Office should not be disturbed.

In such instances, an independent public sector regulator would be in the best position to investigate such transgressions and determine both disciplinary action and provide recommendations on potential reform to internal processes and financial management.

The Public Service Commissioner

The role of the Public Service Commissioner is not one of enforcement but more one of evaluation, facilitation and promotion in relation to the Australian Public Service (APS) (although the Commissioner can investigate breaches of the APS Code of Conduct and make recommendations).

Under the PS Act, responsibility lies with the agency head to establish procedures for determining fraud and breaches of the APS Code of Conduct. At the same time, however, the Commonwealth's fraud control policy does not provide any specific guidance to agencies as to whether they should be contemplating a prosecution using the APS Code of Conduct or whether they should resort to administrative remedies such as the disciplinary procedures of the PS Act.³¹ Guideline 4 of the *Commonwealth*

31 Roberts, P, *Don't Rock the Boat: the Commonwealth National Integrity System Assessment*, Centre for Applied Philosophy and Public Ethics, Charles Sturt University, 2004, p. 18.

Fraud Control Guidelines 2002 states that agencies should 'consider prosecution in appropriate circumstances in accordance with the *Prosecution Policy of the Commonwealth*.³²

In instances where there are concerns about the conduct of an agency head in relation to provisions within the PS Act, such concerns should be raised with the Prime Minister or Secretary of the Department of the Prime Minister and Cabinet, or the Public Service Commissioner. Provisions under paragraph 41(1)(f) of the PS Act enable the Commissioner to inquire into alleged breaches of the Public Service Code by agency heads and to report the results of such enquiries (including recommendations for sanctions where relevant) to the appropriate authority being the Prime Minister if the agency head is a secretary or agency minister if the agency head is the head of an Executive Agency.³³ The Commissioner does not have the power to enforce recommendations.

Strengthening public sector accountability

The lack of a formalised, centralised, statutory authority with enforcement powers has ensured that addressing an alleged contravention remains a matter largely for the agency minister and the relevant agency head. There is no ASIC-type body with the power to investigate, report and enforce disciplinary punishment against alleged breaches of the responsibilities and requirements of agency heads and ministers in regard to delegation and authorisation.

This reality has raised questions about the appropriateness, independence and effectiveness of current responses which are largely internal and informal, particularly in instances where the relevant minister and/or agency head are implicated in the original alleged indiscretion.

Ministers should be subject to the reference of a report to the Prime Minister and Parliament, where they will be held accountable. Officials are another matter, since it should not be the function of the Prime Minister or Parliament to discipline or penalise them.

The lack of a formalised mechanism whereby independent investigation and inquiry is undertaken potentially leading to enforceable action by way of enforceable undertaking, retraining, reprimand, discipline, or punishment of such officials, has the potential to undermine efforts to realise an effective, transparent and accountable financial and operational framework.

5.4 The New Zealand State Services Commissioner

The New Zealand State Services Commissioner has a regulatory function.

32 Minister for Justice and Customs, *Commonwealth Fraud Control Guidelines*: Issued by the Minister for Justice and Customs as Fraud Control Guidelines under Regulation 19 of the Financial Management and Accountability Regulations 1997, May 2002.

33 *Public Service Act 1999*, s. 31(3)(a) and (b).

In a 2007 review of international examples of best practice in achieving civil service accountability, the New Zealand model was identified as having done more than any other system to make an effective distinction between ministerial and official responsibilities workable.³⁴ A 2001 New Zealand ministerial review declared that one of the greatest achievements of the reform is that 'accountability is taken seriously by the system'.³⁵

The State Services Commissioner has three roles, derived from the State Sector Act, that directly or indirectly affect the performance of the departments that make up the Public Service. The Commissioner:

- appoints and employs the chief executives of Public Service departments on behalf of the Crown;³⁶
- reviews the performance of Public Service chief executives on behalf of their responsible ministers; and
- investigates and reports on matters relating to the performance of government departments.

Even though chief executives are employed by the State Services Commissioner, each works for a responsible minister. Ministers set the broad agenda for departments which are, increasingly, translated into a Statement of Intent agreed between minister and chief executive.

The Commissioner reviews the performance of each chief executive, in terms of both their achievement of results and investment in the capability of their organisations, on behalf of the responsible minister. The Commissioner reports on their performance to the responsible minister. Within the constraints of the respective statutory authority of Commissioner and chief executives, the Commissioner manages the performance of chief executives. The annual assessment conducted by the Commissioner may result in a chief executive's contract not being renewed or more serious sanctions. The Commissioner has the power, with the approval of the cabinet, to dismiss a chief executive.

34 The study considered the state of the civil service in Australia, New Zealand, the UK, Singapore, the US, Denmark, Finland, and Sweden, France and the Netherlands, the Scottish Executive and Welsh Assembly Government. (Lodge, G. & Kalitowski, S, *Innovations in Government: International perspectives on civil society reform*, Institute for Public Policy Research, 2007). www.ippr.org.uk/publicationsandreports/publication.asp?id=538 (accessed 20 April 2008).

35 Ministerial Advisory Group, *Report of the Advisory Group on the Review of the Centre*, November 2001, p. 14. www.ssc.govt.nz/upload/downloadable_files/review_of_centre.pdf (accessed 20 April 2008).

36 Under section 35 of the *State Sector Act 1988*, the State Services Commissioner appoints and employs the Public Service chief executives on behalf of the Crown. The Commissioner, therefore, acts as a buffer between ministers and the Public Service and the custodian of the boundary between politics and public management. In this way, the political neutrality of the Public Service is reinforced (State Services Commissioner, *Political Neutrality: Fact Sheet 3: The Relationship between the Public Service and Ministers*. www.ssc.govt.nz/display/document.asp?docid=6510&pageno=1#P9_0 (accessed 21 April 2008).

5.5 Private sector regulation – ASIC, ACCC and APRA

In addition to the consideration of domestic and New Zealand public sector practices above, the regulatory practices applied in the private sector reveal a range of approaches that could be adapted and applied to the public sector.

An effective enforcement process is crucial for ensuring compliance with the law. Regulation of the private sector is grounded in ANU Professor John Braithwaite's regulatory design – 'ascending from voluntary compliance to verbal warnings, the cancellation of licences, and prosecution as a last resort'.³⁷ The regulatory approach of each body is distinct. The approach taken by ASIC is that of 'enforcement supported by education' whereas the focus of the Australian Prudential Regulation Authority (APRA) is that of 'supervision supported by enforcement'.³⁸

The three regulators, APRA, ASIC and the Australian Competition and Consumer Commission (ACCC) rely on a targeted approach. The ACCC assess the costs and benefits of prosecution on a case-by-case basis according to the likely, or actual, impact on consumers. It targets trade practices that are most injurious to consumer interests and, by extension, those companies with the market power to have this effect.

ASIC guides the compliers, influences the opportunists, and prosecutes those who engage in improper and illegal behaviour. It targets providers based on their actions, not their position in the market.³⁹ In relation to breaches of the *Corporations Act 2001* (Corporations Act) auditing and accounting requirements, ASIC can make orders to require compliance; institute legal proceedings which can produce outcomes that carry heavy civil and criminal penalties; direct companies to prepare and lodge reports; seek injunctions to restrain contravention of the Corporations Act; and investigate matters where it believes the Corporations Act or other corporate laws have been broken.⁴⁰

Australian Securities and Investments Commission

ASIC has a range of investigative and enforcement powers that range from compliance tools including persuasion and education as well as negotiation and settlement as an alternative to formal court proceedings, to inspections, investigations and examinations. At last resort, ASIC has the power to pursue civil penalties, banning orders and criminal penalties. ASIC seeks to strike a balance between

37 Grant, R, *Australia's Corporate Regulators – the ACCC, ASIC and APRA*, Research Brief no. 16, 2004–05, 14 June 2005, p. 22.

38 Grant, R, *Australia's Corporate Regulators – the ACCC, ASIC and APRA*, Research Brief no. 16, 2004–05, 14 June 2005, p. 26.

39 Grant, R, *Australia's Corporate Regulators – the ACCC, ASIC and APRA*, Research Brief no. 16, 2004–05, 14 June 2005, pp 31– 32.

40 Treasury, *Strengthening the financial reporting framework. Part 10: Enforcement issues*, 2002. www.treasury.gov.au/documents/403/HTML/docshell.asp?URL=Ch10.asp (accessed 18 April 2008).

applying measures of deterrence with that of striving to achieve compliance through cooperation.

ASIC applies a framework of penalties which seek to operate as a credible deterrent against contravention of the continuous disclosure regime. In this regard there are four types of penalties that may be imposed in relation to contravention of the continuous disclosure regime: removal of an entity from the official list of its listing market by the relevant market operator; financial penalties; adverse publicity; and imprisonment (in relation to individuals convicted as accessories to a criminal contravention by a disclosing entity of the continuous disclosure provisions of the Corporations Act).

Financial penalties and adverse publicity are characterised by a high degree of flexibility and may be applied to fit the circumstances of a much wider range of contraventions than de-listing and imprisonment. Such flexible penalties are therefore more likely to 'operate as a credible deterrent against a wide range of contraventions of the regime.'⁴¹ Indeed, ASIC and the ACCC rely on 'naming and shaming' whilst publicising successful and proposed prosecutions engenders public confidence in their role, and acts as an important deterrent.⁴²

A 1999 research of the ASIC penalties regime established that whilst civil penalties for the enforcement of directors' duties were available to Australian securities regulators from 1993, they were rarely used for reasons of resource constraints, relations with other regulatory agencies, availability of alternative sanctions, and concerns about the utility of civil penalties.⁴³

Conclusion

A primary tenet of good governance is that of a professional public service in which its leadership exercises its powers and responsibilities effectively and ethically and is held to account when transgressions occur.

The accountability gap in the existing enforcement mechanisms detailed in this report demonstrates the need for a public sector regulator which has sufficient flexibility to carry out an enforcement function by way of a range of enforcement options in order that the seriousness of the offence and best way to address a contravention is taken into account.

To perform its role effectively, such a regulator needs strong and comprehensive enforcement powers that promote an efficient regulatory system for the public sector. Persuasion, education and encouraging compliance through negotiation, settlement

41 Treasury, *Strengthening the financial reporting framework. Part 8: Continuous disclosure*, 2002.

42 Grant, R, *Australia's Corporate Regulators – the ACCC, ASIC and APRA*, Research Brief no. 16, 2004–05, 14 June 2005, p. 32.

43 Gilligan, G., Bird, H. & Ramsay, I, *The Efficacy of Civil Penalty Sanctions under the Australian Corporations Law*, Australian Institute of Criminology, November 1999. www.aic.gov.au/publications/tandi/ti136.pdf (accessed 17 April 2008).

and adverse publicity should be the primary enforcement mechanisms. Prosecution resulting in civil or criminal penalties should be a last resort.

Indeed, in recognising the importance of encouraging a culture of self-correction, as a means of strengthening the current compliance framework, a requirement to publish the results of agency compliance reporting could be introduced. Such reporting should focus on documenting remedial efforts promoting a rectification approach rather than a punitive one.

While it is critical that agencies take appropriate action, either administrative or criminal, the focus should be on improving financial management and ensuring that, where compliance breaches occur, they are disclosed along with the steps taken to address the issue. Such a mechanism would assist to encourage compliance.

I have discussed my views with Finance. Finance recognises that the concept of a regulatory body established to ensure compliance with financial obligations has two aspects. Firstly, how agencies such as the Prime Minister and Cabinet and Finance can compel agencies in relation to the directive responsibilities of the two agencies and secondly, whether an alternative or in addition, an independent body such as the APSC or another independent body, could have the ability to impose administrative penalties and regulate agency behaviour.

I recognise that rather than establish a new and separate statutory body, Finance itself could be explicitly recognised as a regulator as well as a central policy agency. A 'regulator' unit could be established within Finance itself. This approach would acknowledge that Finance can legitimately follow up on agency compliance issues and strengthen the current compliance regime rather than produce a new and external structure. Further consideration should be given to the enforcement powers aspect of such an approach and particularly to the question of self-regulation.

A 'regulator unit' in Finance would have the benefit of consolidating all the compliance related areas of Finance into a single area. The regulator unit would be responsible for the development of compliance policy, management of the Compliance Certificate and related processes, to respond to concerns of the JCPAA, the F&PA and ANAO and provide advice on compliance and follow up on agency compliance issues.

While there are clear benefits in consolidating all compliance responsibilities into a single unit within an existing agency, the ability of such a unit to act impartially and independently in instances where Finance itself is non-compliant would have to be clearly demonstrated. There is the danger of Finance being judge, jury and executioner in instances where its own finance directives are the issue.

In a similar vein, if a public sector regulatory function were to be established in the APSC, mechanisms would need to be established to ensure impartiality and independence in dealing with instances of alleged non-compliance from within the APSC.

In establishing a penalty regime for a public service regulator, consideration should be given to the existing powers and penalties applied by the Ombudsman, APSC and

Auditor-General and views of government agencies including ASIC in allocating appropriate penalties for the public sector. Specifically, the powers of ASIC in relation to breaches of the Corporations Act require closer scrutiny.

One important point for those seeking an excuse such as cost to reject my proposal for a public sector regulator – it would be a mistake to assume that such a regulator need be as costly or large as (say) ASIC.

Recommendation 37: That the Government establish a Public Sector Regulator focussed on financial administration and management matters, with strong and comprehensive enforcement powers that promote an efficient regulatory system for the public sector. Persuasion, education and encouraging compliance through negotiation, settlement and adverse publicity should be the primary enforcement mechanisms. Prosecution resulting in civil or criminal penalties should be a last resort.

5.6 Compliance certificates

As discussed above, greater attention to legislative compliance led to the introduction of the Chief Executive's Annual Certificate of Compliance with specified elements of the financial management framework. As part of strengthening the compliance framework, the Department of Finance and Deregulation could prepare an aggregate analysis of all certificates of compliance and advise agencies, and potentially Parliament, on overall trends.⁴⁴

Such a mechanism would provide Finance and potentially Parliament with an alert on systemic and framework issues. As this information relates directly to the efficient and effective expenditure of public funds, it must be made available to the Parliament.

Such an initiative would complement Finance's commitment following an ANAO audit of the 2007 Certificate returns to write to the relevant chief executives regarding their responsibilities to investigate compliance failing and suggesting that consideration be given to informing the responsible minister and/or Parliament of the results of the investigation.

To strengthen transparency and accountability, and to ensure that ministers and the Parliament are fully informed about the performance of departments and chief executives, it would be preferable to require this information to be provided as a matter of course. Without a requirement to do so, it essentially provides an incentive for chief executives to keep information regarding the investigation of compliance failing from their minister.

An analysis of trends in compliance would improve awareness and understanding of agency breaches and complement its recommendation that chief executives inform the responsible minister and/or Parliament of the outcome of the investigation. Improving

44 Department of Finance and Deregulation, *Review of Budget Transparency*, Correspondence regarding Questions from Senator Andrew Murray, 23 April 2008, p. 3.

the use of Compliance Certificates would also reduce referrals for investigation and possible enforcement to the public service regulator recommended above.

The following recommendations should be read as to include the heads of the three Parliamentary Departments who are responsible to respective departmental presiding officers in the same manner in which chief executives are responsible to respective ministers.

Recommendation 38: That the Department of Finance and Deregulation prepare an aggregate analysis of all chief executives' Annual Certificate of Compliance and advise agencies, the ministry and the Parliament on overall trends.⁴⁵

Recommendation 39: That the Government develop processes for chief executives informing the responsible minister and the Parliament of the results of investigations into material compliance failings.⁴⁶

5.7 Management accounts

I am not fully acquainted with the practice regarding the production and use of management accounts across all agencies. I make the following general observations. As a means of strengthening financial accountability, improving governance and preventing breaches of the Commonwealth financial framework, it is essential that key stakeholders are kept as informed and updated as possible, with respect to finance information. Given the scale of Commonwealth operations, management accounts are most effective when provided on a by-exception, key information, and focussed basis. The Prime Minister, Treasurer, Finance Minister, other ministers, and agency or departmental executives, should be regularly provided with relevant management accounts as a matter of course by their home departments.⁴⁷ Such a practice ensures that ministers and managers are fully aware of the financial status of their respective agency and are best equipped to make timely and informed decisions.

45 This recommendation includes the three Parliamentary Departments whereby the Department of Finance and Deregulation would advise the respective department, presiding officer(s) and the Parliament on overall trends.

46 This recommendation should be read to include the heads of the three Parliamentary Departments who should be responsible to inform the respective presiding officer(s) and the Parliament of the results of investigations into compliance failings.

47 Management accounting is concerned with the provision of accounting information to managers to provide them with the basis to make informed business decisions that will allow them to be better informed in their management and control functions. The Chartered Institute of Management Accountants Official Terminology states that management accounting requires the 'identification, generation, presentation, interpretation and use of relevant information to inform strategic decisions and formulate business strategy', inform operational decisions, control operations and ensure the efficient use of resources, measure and report financial and non-financial performance. (Chartered Institute of Management Accountants, *Improving decision making in organisations*, 2007, p. 53). www.cimaglobal.com/cps/rde/xbcr/SID-0AAAC564-3902A97E/live/tech_execrep_improving_decision_making_sept_2007.pdf (accessed 29 April 2008).

6 The Outcomes and Outputs framework

My fourth 'big question' was *'How to get better outcomes and results?'*

Correctly, the Federal Government wants a greater focus on outcomes and results, including over the longer term. This requires increased productivity as well as increased effectiveness.

I determined that this review report should address parliamentary committee; ANAO; Finance; Labor and other relevant initiatives/suggestions, and suggest further ways of advancing this cause.

Of particular note are:

- targets and benchmarks, and accountability with respect to performance;
- ongoing highlighting of exceptional policy, performance or agency items to the cabinet, ministers and parliament (both those of a positive and negative character); and
- separate reports for major whole-of-government cross-agency policies.

It has been approximately 10 years since the adoption of the Outcomes and Outputs Framework (the Outcomes Framework) within the practice of accrual budgeting. Respected commentators, both within and outside of government, agree that the application of the Outcomes Framework has largely been a 'work in progress' within the trajectory of Budget reform.¹

The announcement by the Government that it would implement various reforms to the Outcomes Framework is welcomed. This reform agenda represents a positive step forward that will potentially address significant concerns that have been raised as to how the Outcomes arrangements interact with the open and transparent presentation of government activities to the Parliament, and more generally to the public. Progress to date enhancing the 2008–09 Budget Papers is commendable.

The most critical outcome of all is the benefit delivered by the program. Understanding whether the benefit has been maximised and delivered requires pre-setting the objective and how achieving it will be measured, and in what time frame, and then accurately reporting on the outcome or the progress of the program.

To best capture the good intentions of the current government's reform agenda, relating to the Outcomes Framework, the following areas are addressed, and where appropriate advice and analysis is given as to where further improvements should be made:

- Improving the relevancy of Outcome statements;
- Measuring and evaluating the performance of Outcomes and Outputs;
- Enhancing the 'clear read' principle between the Portfolio Budget Statements and Annual Reports;

1 Professor John Wanna, *Through a Glass Darkly: The Vicissitudes of Budgetary Reform in Australia*, Lecture given at the CPA Continuing Professional Development Program, 2007, pp 5–8.

- Highlighting exceptional performance; and
- Whole-of-government reports for major cross-agency policies.

6.1 Improving the relevancy of Outcome statements

There is an obvious need to translate complex agency intentions into a simpler understandable form for ease of communication and focus, but the danger in such distillation is over-simplification or meaninglessness. Since the inception of the Outcomes Framework in 1999–2000 many agencies have formulated broad and potentially meaningless outcome descriptions that counter the Parliament's ability to understand, assess, monitor and approve Government expenditure.² It must also be noted, that at the time of the introduction of the Outcomes Framework, that the problems currently associated with how vague outcomes would become were largely unforeseen, including by Finance.

In the worst cases you have to wonder at the attitude that encourages useless and generalised outcome descriptions, and then ties large appropriations to them, consequently allowing for such wide ministerial and bureaucratic discretion that accountability loses any meaning. Such latitude, especially if rubber-stamped by a supine or Executive-dominated Parliament, can result in legitimacy being confirmed simply because the law does not prohibit such practice.³

A major purpose of outcome statements is that they justify the basis on which the appropriation of funding takes place. For this reason it is imperative that agency outcomes describe concisely, and specifically, the impacts that the Government intends to achieve through the use of allocated appropriations.⁴

Examples of agencies that have had broad Outcome statements include:

- Centrelink (used only 1 broad Outcome statement that covered the delivery of 119 services and other agreements);⁵
- the Department of Finance and Deregulation ('Outcome 2 states 'Improved and more efficient Government operations');
- the Australian Electoral Commission (Outcome 3 states 'An informed community—An Australian community which is well informed about electoral matters'); and
- the Department of Families, Housing, Community Services and Indigenous Affairs (Outcome 3 states 'Families and children have choices and opportunities' whilst Outcome 4 states 'Strong and resilient communities').

Overly broad outcomes undermine transparency and accountability in the presentation of Government expenditure and operations to the Parliament. This issue has been addressed with recommendations over a period of several years by parliamentary committees and

2 Australian National Audit Office, *Application of the Outcomes and Outputs Framework*, Audit Report No. 23, 2006–07, p. 19.

3 As illustrated for instance in *Combet v Commonwealth* [2005] HCA 61 (21 October 2005).

4 Australian National Audit Office, *Application of the Outcomes and Outputs Framework*, Audit Report No. 23, 2006–07, p. 16.

5 For further analysis see: Senate Finance and Public Administration Committee, *Annual reports (No. 1 of 2008)*, 2008, p. 18.

Australian National Audit Office (ANAO) reports.⁶ The recent *Combet v Commonwealth of Australia* case⁷ demonstrates the importance of tightening Outcome statements in order to limit the executive's ability to fund programs that are not included in the appropriation bills.

A comprehensive discussion of issues concerning accountability and allocation of expenditure between the appropriation bills is presented in Chapter 2.

The problem of broad outcome statements also has a flow on effect not just for the transparency of the allocation of the appropriation of funds to agencies, but also for the establishment of mechanisms by which the performance of Government activities can be monitored. This is discussed further in 'Measuring and evaluating the performance of outcomes and outputs' below.

Operation Sunlight

Operation Sunlight commits the Government to addressing the weaknesses identified above by requiring Finance to actively vet outcomes and outputs and ensure cross Government consistency.⁸ According to Finance 'outcomes will be as detailed and meaningful as possible'.⁹

It is commendable that Finance 'intends to establish mandatory and/or minimum requirements and incorporate principles that agencies should follow in determining outcomes under the policy'.¹⁰ A further challenge to Finance will be how this will be implemented and enforced.

Recommendation 40: That the proposed newly devised, or revised, outcome statements for agencies be implemented no later than the 2009–10 Budget.

When outcome statements are provided for review they should include an outcomes summary which provides the rationale behind any proposed changes and how their specificity will produce greater transparency and accountability.

Recommendation 41: That the Australian National Audit Office review the new outcome arrangements including Finance's guidance and new department outcomes, 12 months after the new arrangements are implemented.

6 See Australian National Audit Office, *Application of the Outcomes and Outputs Framework*, Audit Report No. 23, 2006–07, recommendation 1a and 1b, p. 31; Senate Finance and Public Administration Committee, *Transparency and accountability of Commonwealth public funding and expenditure*, March 2007, recommendation 12, p. 50; Senate Finance and Public Administration Committee, *Annual reports (No. 1 of 2008)*, March 2008, recommendation 3, p. 19.

7 *Combet v Commonwealth* [2005] HCA 61 (21 October 2005).

8 The Hon Lindsay Tanner MP, Minister for Finance and Deregulation, *Interim Response to the Finance and Public Administration Committee report: Transparency and Accountability of Commonwealth Public Funding and Expenditure*, April 2008.

9 Department of Finance and Deregulation, *Implementing Operation Sunlight: Enhancing Budget Transparency*, 2008, p. 3.

10 Department of Finance and Deregulation, *Implementing Operation Sunlight: Enhancing Budget Transparency*, 2008, p. 3.

6.2 Measuring and evaluating the performance of Outcomes and Outputs

Since the introduction of the Outcomes Framework a lackadaisical approach to directing agencies has meant agencies have not been producing detailed and comprehensive outcome and output statements. This has caused difficulties for the objective assessment and evaluation of the performance and delivery of programs by agencies.

One reason for this has been the loss of program detail and specificity in the appropriations process.¹¹ Tied to the current appropriations process is the publication of Portfolio Budget Statements (PBS).

This issue was addressed by the *Transparency* report which stated that in order to overcome the difficulties in assessing agency performance against the allocation of appropriated funds, there is a need for cross-agency consistency of performance measures of cost, quality and timeliness. Systematic evaluation of results against targets also needs to be built into budgeting processes, including through the active involvement of Finance.¹²

Operation Sunlight commits the Government to:

...require the Department of Finance and Deregulation to actively vet outcomes and outputs and ensure-cross government consistency. Results will be described by target for the current year and forward estimates, the expected outcome for the previous year and the actual result for the previous year. Quantity, timeliness, and cost measures will be developed and tracked over time. Outcomes will be as detailed and meaningful as possible.¹³

Operation Sunlight also states that the Government will:

Instigate a systematic program of evaluation of results against targets. This will be done by Finance and be subject to performance audits by the Australian National Audit Office.¹⁴

As evidenced by Finance's revisions to the format of the 2008–09 PBS there are encouraging signs that the level of detail provided in PBS will be improved to enable a clearer picture of what resources will be available to an agency over a Budget year (known as an 'Agency Resource Statement').¹⁵

Furthermore, Finance has stated that the revised format of the PBS will necessitate more detailed key performance indicators (KPIs).¹⁶ It is imperative that KPIs clearly identify how

11 Senate Finance and Public Administration Committee, *Transparency and accountability of Commonwealth public funding and expenditure*, March 2007, p. 49.

12 Senate Finance and Public Administration Committee, *Transparency and accountability of Commonwealth public funding and expenditure*, March 2007, p. 49.

13 *Operation Sunlight*, p. 5.

14 Department of Finance and Deregulation, *Implementing Operation Sunlight: Enhancing Budget Transparency*, 2008, p. 3.

15 See Department of Finance and Deregulation, *2008–09 Portfolio Budget Statements Constructors Kit: Officer Instruction for Producing PB Statements*, 2008, pp 20–21.

16 See Department of Finance and Deregulation, *2008–09 Portfolio Budget Statements Constructors Kit: Officer Instruction for Producing PB Statements*, pp 32–33.

they will contribute to meeting outcomes.¹⁷ So far there is evidence of this approach being present in Finance's changes to guidance for the presentation of the 2008–09 PBS. The implementation of this guidance will require close attention, particularly where in some agencies very large programs are aggregated under a single output group, with a reduction in related KPIs, a lack of precision, and a lack of credible measurable targets.

In the 2008–09 PBS a major change will be a renewed emphasis on performance reporting that is 'more inclusive and results focussed'.¹⁸ Finance states that:

Generating performance information, specifying results and setting performance targets is an internal exercise for agencies. The performance indicators used by agencies should mirror or build upon those used by the agency in its own internal management, to ensure that operations are working towards government outcomes efficiently and effectively...¹⁹

When setting performance targets agencies are to be conscious of previous years' targets and their progress towards them. Performance targets should not be static, they should grow with improved practices and methods, periodically being evaluated and revised to ensure agencies are achieving the best possible results in contributing towards their outcomes...²⁰

The inclusion of more detailed performance information in the form of KPIs responds positively to the concerns and recommendations put forward by the ANAO.²¹ However, it should be noted that unless KPI targets are both realistic and meaningful it will undermine the value of including KPIs. For example it emerged at the 2008–09 Budget Estimates hearings that the Australian Electoral Commission's target of 95 per cent for the proportion of eligible people on the electoral roll was a static figure based on current reality.²²

Furthermore it is also important that a thorough evaluation takes place of the performance of each agency towards meeting their KPIs and outcome statements. This is discussed below in 'Enhancing the 'clear read' between the PBS and Annual Reports'.

As well as agencies producing more detailed outputs that relate to KPIs that act as markers towards assessing and achieving outcomes: the ANAO has recommended that Finance enhance the integration of the Outcomes Framework into agencies' operations.²³

The ANAO identified that an agency's capacity to implement the Outcomes Framework in order to improve decision making and accountability is enhanced when outcomes and outputs

17 See Australian National Audit Office, *Application of the Outcomes and Outputs Framework*, Audit Report No. 23, 2006–07, recommendation 1, p. 31.

18 See Department of Finance and Deregulation, *2008–09 Portfolio Budget Statements Constructors Kit: Officer Instruction for Producing PB Statements*, 2008, p. 33.

19 Department of Finance and Deregulation, *2008–09 Portfolio Budget Statements Constructors Kit: Officer Instruction for Producing PB Statements*, 2008, p. 32

20 Department of Finance and Deregulation, *2008–09 Portfolio Budget Statements Constructors Kit: Officer Instruction for Producing PB Statements*, 2008. p. 33.

21 See Australian National Audit Office, *Briefing Note No. 1*, 2008, p. 1; and Australian National Audit Office, *Application of the Outcomes and Outputs Framework*, Audit Report No. 23, 2006–07, recommendation 1, p. 51.

22 Finance and Public Administration Committee, Budget Estimates, 29 May 2008.

23 See Australian National Audit Office, *Application of the Outcomes and Outputs Framework*, Audit Report No. 23, 2006–07, recommendation 2, p. 55.

are aligned with organisational structures; and when elements of the Outcomes Framework are integrated with internal performance management regimes.²⁴

As outlined above, Finance's directive to agencies to incorporate KPIs in their own internal management operations is a step in the right direction. Finance's movement towards improving the relevancy of KPIs, and the way they contribute to achieving outcomes is also to be welcomed.

Perhaps a way to further improve the aligning of KPIs to the internal management operations of agencies would be to link them to the performance agreements of SES staff. As Professor John Wanna recently stated:

On performance management and reporting, secretaries, executives and program managers all have incentives to deliver on budget or within budget (even under-budget but certainly not over-budget) rather than seeking to maximise outcomes.²⁵

Professor Wanna's observation highlights the fact that the attention of agencies to meeting outcomes through outputs and KPIs, is at times distracted by other operational pressures. Similarly, although with a slightly different emphasis, the ANAO recommended that:

...agencies review, and where necessary improve: their performance indicators that incorporate better practice characteristics that provide stakeholders with useful and reliable performance information...²⁶

Recommendation 42: That in order to enhance the integration of the Outcomes and Outputs Framework into agency operations and work area business plans that individual SES performance agreements have regard to the achievement of relevant outcomes, outputs and KPIs.

6.3 Enhancing the 'clear read' between the PBS and Annual Reports

A major purpose of the review function of agency annual reports is that they allow evaluation of agencies' progress towards achieving their stated outcomes. Part of this evaluation process must also be linked to the assessment of agencies' performance against their published KPIs. Arguably, the 'clear read' or link between an agency's appropriations and review of whether their stated outcomes have been achieved, is not present in the current content of agency annual reports.

For example this issue was raised by the F&PA Committee. The F&PA Committee analysed Centrelink's *Annual Report 2006–07* and found that little information was provided to explain

24 Australian National Audit Office, *Application of the Outcomes and Outputs Framework*, Audit Report No. 23, 2006–07, p. 52.

25 Professor John Wanna, *Through a Glass Darkly: The Vicissitudes of Budgetary Reform in Australia*, CPA Continuing Professional Development Program, 2007, p. 11.

26 Australian National Audit Office, *Application of the Outcomes and Outputs Framework*, Audit Report No. 23, 2006–07, p. 31.

how Centrelink measured its KPIs and the reasons for failing to meet KPIs.²⁷ This lack of detail inevitably led to difficulties in making an informed assessment of how the agency performed against its stated outputs and outcomes (of which there was only one). The evaluation of results against targets is currently required to be produced by agencies in their annual reports under the *PM&C Guidelines*. However, as stated in *Operation Sunlight*, there remains 'imprecise reporting of targets and little reporting back against key result areas'.²⁸

To alleviate this problem Finance states that by 2009–10 'it is proposed that each year agencies be required to report in their Annual Report against targets set out in their PBS. It is envisaged that such reporting will be against programs'.²⁹ This will potentially enhance the 'clear read' principle between the PBS and Annual Reports, and is to be welcomed. It is also understood that Finance will consult with PM&C to amend the *PM&C Guidelines* as required.

Emphasis should rest with the provision of standardised information that is consistent across all agencies. Current reporting on issues including OH&S, freedom of information and environmental performance in agency annual reports for example, varies considerably between agencies, making analysis between and across agencies an extremely difficult if not impossible task. Standardising informational requirements and allowing some degree of exception reporting would improve the information provided and also reduce internal red tape. The approach of moving such information from one document or medium to another, as suggested by Finance, does not appear to address the provision of inadequate information or reduce the burden on agencies to provide such information in the first instance.

Furthermore, Finance has stated that it will make changes to the 2008–09 PBS whereby an 'Outcome Strategy' will replace the 'Summary of Contributions to Outcomes' diagram used in the previous 2007–08 PBS: with a shorter statement focused on the key strategies to be undertaken in contributing towards each outcome. This document also is intended to develop the 'clear read' principle between the PBS and annual reports.³⁰

Perhaps it would be beneficial if this document is replicated and presented clearly in the annual report of each agency.

Finally, it is also of note that Finance intends to 'instigate a systematic program of evaluation of results against targets that will be subject to a performance audit by the ANAO'.³¹ Furthermore, Finance's intention to publish this information in an 'omnibus report' will potentially provide another valuable input to the Cabinet and the Budget process.

27 Senate Finance and Public Administration Committee, *Annual reports (No. 1 of 2008)*, March 2008, pp 16–17.

28 *Operation Sunlight*, p. 3.

29 Department of Finance and Deregulation, *Implementing Operation Sunlight: Enhancing Budget Transparency*, 2008, p. 4.

30 Department of Finance and Deregulation, *2008–09 Portfolio Budget Statements Constructors Kit: Officer Instruction for Producing PB Statements*, 2008, p. 29.

31 *Operation Sunlight*, p. 4.

6.4 Highlighting exceptional performance

To complement the improved performance reporting arrangements contained in *Operation Sunlight*, there would be merit in developing a system of reporting on exceptional policy, performance and agency items. Highlighting outstanding examples of policy and program development and implementation (both positive and negative) would benefit the performance of other agencies, improve overall public sector productivity and effectiveness and provide greater transparency over the expenditure of public monies.

The ANAO already undertakes performance audits across the public sector. It undertakes independent assessment of selected areas of public administration, and assurance about public sector financial reporting, administration, and accountability. It also seeks to provide an objective assessment of areas where improvements can be made in public administration and service delivery. In addition to its audit functions, the ANAO prepares a range of *Better Practice Guides* to inform public sector agencies of sound practices in key areas of public administration.

As a result, the ANAO has a wealth of skills, information and knowledge regarding exceptional public sector performance (both positive and negative).

Other agencies have skills information and knowledge by topic (for example, the Commonwealth Ombudsman on FOI and or the Public Service Commissioner on the Public Service), while departments and agencies themselves have specific expertise.

There would be merit in the Government considering ways in which exceptional performance could be objectively reported to parliament on a regular or periodic basis, to raise the bar on public administration. This would allow Cabinet and Ministers, amongst others, to more closely monitor outstanding performance across the public sector. Agencies would be able to submit examples of best practice administration of Government policy. The Government could then make recommendations for areas of performance improvement across the public sector.

Recommendation 43: That before 2010 the Government implement an exceptional performance report designed to highlight outstanding public sector performance (both positive and negative). Subject to practical considerations that might dictate otherwise, the report should preferably be presented to Parliament on a twelve month basis.

6.5 Whole-of-government reports for major cross-agency policies

Given the complexities of modern day society, developing and delivering Government policy in the 21st Century is rarely constrained to a single agency. Although one agency may take the lead in intricate policy areas such as climate change and Indigenous affairs, these challenging issues can require input and involvement from a myriad of Government departments and agencies, that all play their part in developing and implementing the overall policy. Every major challenge of public administration – ensuring security, building a strong economy, coping with demographic change and crafting social policy – necessarily requires the active participation of a range of central and line agencies.

In order to fully understand the outcomes of major Government policy initiatives it is vital that performance information on these cross-cutting policy issues is consolidated in a single

report. Without a whole-of-government picture, it is next to impossible to fully grasp how effectively key Government policies are being implemented and managed.

Whole-of-government reports can be broadly distinguished from 'standard cross-agency reports'. These latter reports largely focus on the internal administrative functions of agency operations, which for example include reporting to Parliament on contracts, file lists, leave entitlements and consultants. By contrast, whole-of-government 'integrated reports' include more significant policy measures, outcomes or goals, put in place by Government (for further elaboration and discussion with examples see below).

Timeframes

It is also important to consider the relevant timeframes for the production of whole-of-government reports. In order to maximise the usefulness of the information and indicators presented in whole-of-government reports various timeframes for presentation to Parliament should be applied, for example: on an annual basis; per Parliamentary term (every three years); or on a long-term basis (up to 40 years).

Whole-of-government integrated reports

Examples of policy areas or Government functions where whole-of-government integrated reporting is currently undertaken include:

- State of the Service report – reflects the activities and human resource management practices of APS agencies and outlines some of the key achievements and contributions agencies have made in assisting the Government to meet its policy objectives and achieve its stated outcomes;
- The regular fiscal reporting requirements of the *Charter of Budget Honesty Act 1998* and the FMA Act at the whole-of-government level, for example, the Budget Economic and Fiscal Outlook report, Mid-Year Economic and Fiscal Outlook, and Final Budget Outcome Report (i.e. BEFO, MYEFO, FBO);
- The Intergenerational Report (IGR) also produced under the requirements of the *Charter of Budget Honesty Act 1998*, which is designed to assess the long term sustainability of current Government policies over 40 years following its release;
- FaHCSIA prepare an annual *Indigenous Affairs Budget* which in 2007–08 contains 26 initiatives involving \$815.7 million funding over five years focused on remote housing, early childhood, new education opportunities, health and economic independence; and
- Government energy use – each year the Department of the Environment produces a whole-of-government energy performance report, *Energy Use in the Australian Government's Operations*, which is tabled in Parliament before the last working day of April of each year.

Areas where there is shared delivery responsibility but no common reporting mechanism, suffer from an uncoordinated and piecemeal approach to reporting achievements and

outcomes. The standard budget mechanisms for providing information on continuing performance are ineffective in relation to whole-of-government measures.

For example for two whole-of-government initiatives, the National Heritage Trust (for which an annual report is required under the relevant legislation) and the National Action Plan on Salinity, for which the Government nominated the two delivery agencies (the Department of Environment (DEWHA) and the Department of Agriculture, Fisheries and Forestry (DAFF)), the performance measures are spread between DEWHA and DAFF's PBSs. They are organised differently, reflecting the way in which those programs are managed within the outcome and output structures of the relevant administering departments.

Other examples where there would be benefit in whole-of-government performance reporting are:

- An annual whole-of-government report relating to Government advertising expenditure that details the information stipulated in recommendation 10 of the Senate Finance and Public Administration Committee report *Government advertising and accountability*;³²
- Special appropriations table, which the Government has committed to under *Operation Sunlight* (and which has already happened);³³ and
- Agency carryovers.³⁴

Currently, reporting on the progress and performance measurement of major whole-of-government initiatives is often not available in a consolidated form. Elements of the initiative are reported in separate PBSs and Annual Reports of responsible departments. Guidance from the ANAO concerning cross-agency governance indicates that 'Cross-agency policy development or operational arrangements should not inadvertently result in an accountability gap where responsibility for outcomes is unclear or ambiguous'.³⁵ There would be merit in determining reporting and evaluation arrangements for major whole-of-government budget initiatives at the point at which budget decisions are made. This would remove scope for ambiguity.

Factors worth considering in determining reporting and evaluation arrangements include what initiatives should be included, who would be responsible for reporting (a lead agency?), what would be the structure of a report and whether reporting would be within current mechanisms (such as in the lead agency's Annual Report).

32 Recommendation 10 states that the information to be produced annually is: a total figure for government expenditure on advertising activities; total figures by agency for expenditure on advertising activities; figures for expenditure on media placement by type and media placement by month; and detailed information about major campaigns, including a statement of the objectives of the campaign, the target audience, a detailed breakdown of media placement, evaluation of the campaign including information about the methodology used and the measurable results, and a breakdown of the costs into 'production', 'media placement' and 'evaluative research'. Senate Finance and Public Administration reports, *Government advertising and accountability*, December 2005, pp 104–105.

33 Also see Senate Finance and Public Administration Committee, *Transparency and accountability of Commonwealth public funding and expenditure*, March 2007, recommendation 1, p 18.

34 Senate Finance and Public Administration Committee, *Transparency and accountability of Commonwealth public funding and expenditure*, March 2007, recommendation 5, p 30.

35 Australian National Audit Office, *Cross Agency Governance Guidance Paper No. 7*, July 2002, p. 2.

If the Government considered that particular major whole-of-government initiatives would benefit from consolidated reporting of year-on-year budget progress and performance information this should be determined by ministers when initial funding decisions are made and well before the commencement of the reporting cycle.

Recommendation 44: That the Government implement annual and periodic whole-of-government reporting for major cross-portfolio policies.

COAG-wide joint government reports

Many major issues do not respect political demarcations – they are national (eg indigenous affairs) or regional (eg the Murray Basin) in scope. Many such issues are ones with joint inter-governmental responsibility. The Government has embraced the term ‘seamless economy’ that has a one-nation ring to it. Self-evidently there are issues of such national significance, and where implementation involves shared Commonwealth-State responsibility, that COAG governmental reports are required.

Examples of nationally significant issues that are presently dealt with by COAG include:

- Productivity, Education, Skills and Early Childhood;
- Business Regulation and Competition;
- Health and Ageing;
- Climate Change and Water;
- Infrastructure;
- Housing;
- Indigenous Reform;
- Alcohol abuse; and
- Gambling.

In order to evaluate the performance of COAG activities (including: memorandums of understanding; intergovernmental agreements; and the work of Ministerial Councils) it would be beneficial for the Commonwealth Government to collaborate with its state and territory counterparts to produce COAG-wide cross-governmental reports.

These reports would be tabled on an annual or periodic basis. Annual reports should be available prior to each COAG meeting which would then enable all COAG participants to access comprehensive analysis of the performance of COAG outcomes; this analysis could then be used to improve the decisions made relating to future policy directions across Federal and State jurisdictions. These would generally be expected to be public reports.

Recommendation 45: That the Government agree with COAG a process for selected annual or periodic whole-of-Australia reporting for major national concerns.

Appendix 1

OPERATION SUNLIGHT

Enhancing Budget transparency

Transparency and good governance

After extensive consultation with a range of academics, journalists and professional analysts, Labor has developed a practical suite of measures to enhance Budget transparency which could be implemented within existing resources. Contributions were drawn from the following people who chose to provide their views in a private capacity:

- Pat Barrett – former Commonwealth Auditor-General.
- Ross Gittins – Economics Editor, Sydney Morning Herald.
- Grant Bellchamber – Australian Council of Trade Unions.
- Des Moore – Director, Institute for Private Enterprise.
- Professor Stephen Bartos – National Institute for Governance, University of Canberra.
- Peter Davidson and Andrew Johnson – Australian Council of Social Services.
- Steven Munchenberg – Deputy Chief Executive Business Council of Australia.
- Saul Eslake – Head of economics, Australia New Zealand Bank.
- Stephen Koukoulas – Chief strategist, TD Securities.
- Charles Berger – Australian Conservation Foundation.
- Geoff Carmody – former Director, Access Economics.
- John Wanna – Australia New Zealand School of Government, Australian National University.
- Senator Andrew Murray – Australian Democrats spokesperson for Taxation, Finance & Corporate Affairs.
- Michael Potter – Head of economics and tax, Australian Chamber of Commerce and Industry.

Ideas for budget reform were also drawn from *A Blueprint for South Australia's Future, Business SA, 2006*.

The following reforms will improve the quality, transparency and consistency of Budget reporting:

- Tightening the outcomes and outputs framework.

- Changing Budget Papers to improve their readability and usefulness.
- Improving the transparency of estimates.
- Expanding the reach of Budget reporting.
- Improving Intergenerational reporting.

Labor is committed to improving Budget transparency and accountability.

Tightening the outcomes and outputs framework

Issues:

The Budget is structured around outcomes and outputs. Money is spent on outcomes while outputs and programs sit under the outcomes. Ministers approve their own outcomes. Some outcomes are so broad and general as to be virtually meaningless for Budget accounting purposes leading taxpayers to only guess what billions of their dollars are being spent on. Some of the more incomprehensible examples are:

- Outcome 4 for the Department of Family and Community Services is “Families and children have choices and opportunities – Services and assistance that: help children have the best possible start to life; promote healthy family relationships; and help families adapt to changing economic and social circumstances and take an active part in the community”.
- \$454 million is allocated to the Department of Employment and Workplace Relations for “Higher pay, higher productivity”.
- \$2.1 billion is allocated to the Department of Transport and Regional Services for “Assisting regions to manage their own futures”.

There is also imprecise reporting of targets and little reporting back against key result areas. Loose outcome descriptions can also foster incentives for money to be shifted between outcomes for political purposes or for spending such as government advertising to be undertaken for overt political purposes without parliamentary approval.

- For example, Audit Report No. 31 2006 on the Roads to Recovery Program found that money had been shifted from one outcome - “a better transport system for Australia” to another outcome “greater recognition and development opportunities for local, regional and territory communities”. This is open slather for political pork-barrelling.
- For example, in *Combet and Roxon v Commonwealth*, the Government argued that the PBS is irrelevant in understanding what is contained in appropriations. Instead it was claimed that the broad Outcome appropriation description of ‘higher productivity, higher pay workplaces’ was enough to justify the \$55 million Industrial relations advertising campaign. The advertising campaign was not mentioned in the Portfolio Budget Statement (PBS).

The Government’s outcomes and outputs framework was intended to shift the focus of financial reporting from inputs (programs, expenses, and recipients) to outputs and outcomes i.e. actual results. While this is worthy in theory, it has not worked.

Basic information on inputs was lost in the changeover, and reporting of outcomes is seriously inadequate.

Labor will:

- Require the Department of Finance and Administration to actively vet outcomes and outputs and ensure cross-government consistency. Results will be described by target for the current year and forward estimates, the expected outcome for the previous year and the actual result for the previous year. Quantity, timeliness, and cost measures will be developed and tracked over time. Outcomes will be as detailed and meaningful as possible.
- Instigate a systematic program of evaluation of results against targets. This will be done by the Department of Finance and Administration and be subject to performance audit by the Australian National Audit Office.
- Develop more detailed and binding descriptions of the content of appropriations in the PBS. This would help strengthen the role of Parliament under sections 81 and 83 of the Constitution in scrutinising and approving appropriations.
- Include in the Budget Papers a review and report back on the performance of funding allocations from the previous year's budget including whether savings have been met.

Changing Budget Papers to improve their readability and usefulness

Issues:

Budget Paper No. 1 (BP No.1) is the main Budget Paper but its focus is somewhat confused. It contains information on the immediate economic outlook (Statement 3) as well as information on longer-term issues to do with prosperity and sustainability (Statement 4). These statements may be better placed in a separate Budget Paper that focuses more squarely on the Federal Government's strategic fiscal objectives as well as non-budget policies related to longer-term performance.

BP No. 1 lacks detail on classes of recipients, sources of revenue and which classes get assistance, under what conditions, average amounts paid and results achieved. There is no analysis of the impact of the tax and welfare system on income groups much less the non-achievement of savings. Information is hard to piece together given that portfolio responsibilities for income support are split between the Departments of Employment and Workplace Relations, Family and Community Services and Education Science and Technology.

There is insufficient mapping of spending by agencies on particular programs between Budget Papers and the PBS. Expenses are classified on two different bases. The PBS classify expenses by outcome. BP No.1 classifies by function or

purpose. The two are not reconciled. Transparency is further reduced where responsibilities sit across portfolios.

- For example, spending on the Housing and community amenities function and the three sub-functions (see BP No. 1, 2005-06 p6-13) traverses programs in the portfolios of Defence, Transport and Regional Services and Family and Community Services. There are no program descriptions. Instead, users have to try their luck hunting programs through at least three different sets of PBS.

There are mixed views about the appropriate accounting standard used in the Budget Papers – Government Finance Statistics (GFS) which applies to the public sector or Australian Accounting Standards (AAS) which applies to the private sector. Options to standardise the two are currently being examined. Rather than prolong the debate, it may make more sense to settle for one standard in the Budget Papers and be done with it, thereby avoiding the problem of politicians ‘cherry-picking’ information depending on the result they want. Other information would not be lost but go to an Appendix.

The Budget Papers do not treat the GST as a Commonwealth tax. Both the Australian Bureau of Statistics and Auditor-General agree that constitutionally, the GST is a Commonwealth tax because the GST is imposed and administered under Commonwealth legislation. Conveniently for the Government, not reporting it understates Commonwealth taxation.

Labor will:

- Remodel BP No. 1 to focus on information that helps to assess the merits of government spending and tax levels. This would include information on the distribution of welfare, health and education benefits between income groups, and the taxes paid by such groups. Further advice will be sought including making Statements 3 and 4 a separate Budget Paper.
- List programs in the Budget Papers that sit under sub functions including forward estimates. This program information would be cross-referenced to the PBS. Individual PBS would contain a ‘contra’ reference back to the Budget Papers.
- Make GFS the standard in the Budget Papers. AAS material would be provided in an Appendix with additional schedules.
- Count the GST as a Commonwealth tax.

Improving the transparency of estimates

Issues:

Material estimation errors are often 'hidden' as parameter variations and there is no system of continuous fiscal disclosure to inform users of material variations.

Estimation errors are a natural part of implementing new policy. Unfortunately, estimation errors from policy decisions such as increased take-up are often treated as 'parameter variations', disguising the real impact of policy decisions. The Private Health Insurance rebate is a case in point. The 1998 measure or 'policy decision' was estimated to cost \$5.2 billion over the first four years of its operation. It actually cost \$6.6 billion. The increase in cost is counted as a 'parameter variation'.

Transparency of estimates is also not aided by agencies not consistently reporting when expenditure slips and the forward estimates are 'rephased' or adjusted. This sometimes allows agencies and Ministers to announce spending and then reannounce that same spending ad infinitum.

Stable economic policy is not served by sudden jumps in revenue or expenses throwing out the Budget bottom line between key economic statements. This is made worse when markets and commentators are caught out by the size of the fluctuations. The private sector operates under rules of continuous disclosure. Why shouldn't the public sector?

The Department of Finance and Administration publishes monthly financial statements for the current financial year in a form consistent with the Budget estimates (fiscal balance, the underlying cash balance and the net operating result). The date of publication varies significantly.

Unfortunately, there aren't even mandated reporting dates for key publications such as the Mid-Year Review and the Australian Government's Monthly Financial Statement. For example, the July and August 2005 reports were released on 30 September 2005.

Labor will:

- Require Treasury and Finance to publish material changes in revenue or expenses on their web sites. Consolidated and updated fiscal and cash balances will be produced and published on both the Treasury and Finance web sites every 3 months.
- Mandate regular publication dates for key economic documents such as the monthly financial statement.

Expanding the reach of Budget reporting

There are a number of areas of budgeting that be made more transparent – Special accounts, Standing appropriations, Tax expenditures and the Contingency reserve.

Issues:

Special accounts grant a right to departments to draw from the Consolidated Revenue Fund. While there are guidelines on the management of such accounts and they are reported in agency PBS there is no consolidated list of such accounts and their balances.

Standing or special appropriations operate under their own legislation and are usually uncapped and entitlement-driven (e.g. most social security payments). In Audit Report No.15 2004-05, Financial Management of Special Appropriations, the ANAO found “widespread shortcomings...in the management and disclosure of Special Appropriations”. They account for about 80 percent of Commonwealth government spending compared to about 25 percent in the UK and have been growing over time.

Tax expenditures involve granting certain taxpayers, activities or assets more favourable tax treatment than applies to others. They are not subject to the same budget processes or trade-offs as expenditure programs. Once in, tax expenditures are hard to change or remove. ‘Equity’ implications of tax expenditures flowing to high income earners are rarely assessed (25 percent of households don’t have access to tax expenditures because they don’t pay tax). In 2005-06, tax expenditures were around \$31 billion against total expenses of \$206 billion. Total spending would be 15 percent higher if tax expenditures were added back. It may be even higher as many tax expenditures are simply not estimated by Treasury.

For example:

- certain taxpayers can be released from a tax liability where the liability would cause serious hardship (2005 Tax Expenditures Statement, p57). No cost is given.
- certain in-house loan benefits provided to employees to meet employment-related expenses are exempt from fringe benefits tax (2005 Tax Expenditures Statement, p125). No cost is given.

The *contingency reserve* is a global reserve which is supposed to allow for: amounts not yet allocated to individual programs; the tendency to underestimate costs of existing programs in future years and the tendency to overestimate administered item expenses in the early years as programs get up to speed. In the lead-up to elections these ‘hidden’ allocations can be very important. There is no detail on year by year fluctuations.

Labor will:

On Special accounts –

- Require the Minister for Finance no later than 31 August each year to table a consolidated register of special accounts. This would detail the relevant statutory provisions, date of establishment/duration, purpose, and amount expended at the close of the financial year. This is consistent with amendments already proposed to the Financial Framework Legislation Amendment Bill (No. 2) 2005 and rejected by the Government.

On *Standing or special appropriations* –

- Consistent with the above, establish a register of standing appropriations.

On *tax expenditures* –

- Require an independent up-front audit and assessment of existing concessions.
- Require more detailed specification of what is to be achieved from tax expenditures, set in place processes for their periodic review and notionally allocate such expenditures to functions and sub functions to facilitate comparisons with other expenditure.

On the *contingency reserve* –

- Require a reconciliation table by sub function for changes across the forward estimates. This would be produced in the Budget and at Mid Year Economic and Fiscal Outlook.

Improving Intergenerational reporting

Issues:

The Treasurer produces an Intergenerational Report every five years as per the provisions of the *Charter of Budget Honesty Act 1998*. The Charter was a first attempt to publish more demographic information every five years and to set out costing arrangements during the election campaign. Given the increased focus on demographic issues, the Charter is now in need of a revamp.

The Charter doesn't disaggregate long-term spending pressures by program and arguably five years is too long between updates. Insufficient attention is paid to demographic pressures in costing new policies. Many government programs may be affordable now but are set to grow steeply beyond the forward estimates at a time when workforce participation rates and the tax base decline. The current forward

estimates do not capture such trends early enough. The current forward estimates period should be extended to six years for programs likely to be subject to demographic pressures.

The Charter fails to acknowledge emerging trends in the private sector where corporations are increasingly taking account of the longer-term environmental and social costs and benefits of their actions. More can be done via integrated triple-bottom-line analysis.

Policies of governments and oppositions are not costed fairly under the Charter. The Charter is heavily biased in favour of the government of the day including the release of the Pre-election economic and fiscal outcome up to 10 days into the election campaign with no opportunity for independent scrutiny. Access to costing resources for the Opposition only applies during the heat of an election campaign whereas the Government has access year-round.

Labor will:

- Improve the co-ordination of the Commonwealth's long-term modelling capability to reduce long-term risks to the Budget.
- Require all expenditure measures at risk of long-term growth to be subject to mandatory assessment at the time a proposal is considered.
- Make it mandatory that all new programs subject to significant demographic risk be assessed and reported over a 40 year timeframe consistent with the Intergenerational Report.
- Extend the forward estimates period to six years for programs likely to be subject to demographic pressures to make it easier to identify emerging cost pressures earlier.
- Investigate the utility of a whole-of-government triple-bottom line (economic, environment and social) chapter in the Intergenerational report.
- Revitalise the *Charter of Budget Honesty Act 1998* including by legislating to allow the Government or Opposition to request the Secretaries to the Departments of the Treasury and Finance to prepare a costing of any policies within 12 months of the last day for issue of the writs for a general election to the end of the caretaker period. Agreed costings would then be publicly released.
- Have the IGR produced every three years with greater disaggregation at the program level.

Appendix 2

Recommendations

Set out below are ANAO's recommendations.

- Recommendation No.1**
Paragraph 2.23
- ANAO *recommends* that the Department of the Treasury:
- (a) develop an approach for the conduct of an ongoing prioritised review of the existing program of tax expenditures; and
 - (b) publish for each tax expenditure information on the timing and outcome of the review.

Agency response: Treasury agreed to part (a) and agreed with qualification to part (b).

- Recommendation No.2**
Paragraph 2.38
- ANAO *recommends* that the Department of the Treasury examine and advise Ministers on options to better integrate the consideration of outlays and tax expenditures in the annual Budget process.

Agency response: Treasury agreed.

- Recommendation No.3**
Paragraph 2.49
- ANAO *recommends* that the Department of the Treasury develop standards to govern the integrated reporting of outlays and tax expenditures under the Charter of Budget Honesty, drawing on international developments in this area.

Agency response: Treasury agreed with qualification.

**Recommendation
No.4
Paragraph 3.39**

ANAO *recommends* that the Department of the Treasury promote more comprehensive reporting on taxation expenditures by:

- (a) liaising with Commonwealth entities that collect revenue to identify all entities that also administer forms of relief from Commonwealth taxes, including tax expenditures; and
- (b) developing arrangements, as part of the preparation of the annual Taxation Expenditure Statement, to obtain relevant data from entities outside the Treasury portfolio.

Agency response: Treasury agreed. The ATO agreed with part (b).

**Recommendation
No.5
Paragraph 4.16**

ANAO *recommends* that the Department of the Treasury and the Australian Taxation Office identify opportunities to develop estimates of large or otherwise significant tax expenditures using the revenue gain method.

Agency response: Treasury agreed.

**Recommendation
No.6**
Paragraph 4.49

ANAO recommends that the Department of the Treasury:

- (a) develop an approach to prioritise improvements to the reliability of published tax expenditure estimates;
- (b) examine options for disclosing in the TES information on the reliability of individual tax expenditure estimates;
- (c) work with the Australian Taxation Office to develop reliable models to estimate the revenue forgone for existing tax expenditures that are large or otherwise significant; and
- (d) when developing advice for Ministers on policies that are expected to result in a tax expenditure, assess options for the reliable measurement of the effect of the proposed measure.

Agency response: Treasury and the ATO both agreed with parts (a), (b) and (c) and agreed with qualification to part (d).