

## **Performance Audit Report No. 9 (2014-15)**

# Design and Conduct of Third and Fourth Funding Rounds of Regional Development Australia Fund

## **Introduction**

- 2.1 Chapter 2 focuses on the Joint Committee of Public Accounts and Audit (JCPAA) review of Australian National Audit Office (ANAO) Report No. 9 (2014-15), *Design and Conduct of the Third and Fourth Funding Rounds of the Regional Development Australia Fund*, Department of Infrastructure and Regional Development. The chapter comprises:
- an overview of the report, including the audit objective, scope and criteria; audit conclusion; and audit recommendations and agency response
  - Committee review
  - Committee comment

## **Report overview**

- 2.2 The Regional Development Australia Fund (RDAF) was established in early 2011 as a nationally competitive, merit-based grants program with discrete funding rounds. Four RDAF funding rounds were delivered between 2011 and 2013, with the third and fourth funding rounds being

conducted between October 2012 and June 2013.<sup>1</sup> Table 2.1 sets out the number of applications approved and funding over the four rounds.

Table 2.1 RDAF applications and funding over rounds one to four

Funding round	Date round opened	Applications approved	Funding approved
Round one	3 March 2011	35	\$149.7 million
Round two	3 November 2011	46	\$199.8 million
Round three	26 October 2012	79	\$31.1 million
Round four	26 October 2012	42	\$195.2 million
<b>Total</b>		<b>202</b>	<b>\$575.8 million</b>

Source ANAO, *Audit Report No. 9 (2014-15), Table 1.1, p. 38*

2.3 Administration of RDAF was initially allocated to the then Department of Regional Australia, Regional Development and Local Government, which became the Department of Regional Australia, Local Government, Arts and Sport (DRALGAS) in December 2011.<sup>2</sup> Since September 2013, following the change of government, RDAF has been administered by the Department of Infrastructure and Regional Development (DIRD).

2.4 The ANAO conducted a previous inquiry into the first RDAF funding round in September 2012.<sup>3</sup>

## Audit objective, scope and criteria

2.5 The objective of the ANAO audit was to assess the effectiveness of the design and conduct of the third and fourth RDAF funding rounds. The scope of the audit included the processes by which proposals were sought and assessed, and successful projects were approved for funding.

2.6 To form a conclusion against the audit objective, the ANAO adopted the following high-level criteria:

- application and eligibility assessment processes promoted open, transparent and equitable access to the available funding;
- the merit assessment process identified and ranked in priority order those eligible applications that best represented value

1 ANAO, *Audit Report No. 9 (2014-15), Design and Conduct of the Third and Fourth Funding Rounds of the Regional Development Australia Fund, DIRD*, p. 14.

2 The ANAO report refers to DRALGAS as the department then responsible for the design and conduct of RDAF rounds three and four, and to DIRD as the department consulted by the ANAO for the purposes of the audit and now responsible for implementing the report recommendations. For further clarification of this matter, see ANAO, *Audit Report No. 9 (2014-15)*, p. 11.

3 ANAO, *Audit Report No. 3 (2012-13), Design and Conduct of the First Application Round for the Regional Development Australia Fund, DRALGAS*.

with public money in the context of the program objectives and desired outcomes;

- the Minister, as decision-maker, was well briefed on the assessment of the merits of eligible grant applications, was provided with a clear funding recommendation and the reasons for the funding decisions were transparent (consistent with the requirements of the broader financial framework and the grants administration framework); and
- the distribution of funding in geographic and electorate terms was consistent with the program objectives and guidelines, and was consistent with funding being awarded on the basis of competitive merit.<sup>4</sup>

## Audit conclusion

2.7 The ANAO's overall conclusion was as follows:

The assessment and selection process as it was described in the program guidelines reflected a sound approach. However, in the manner implemented, the stages were not well integrated in that each step informed the next in only a limited way. As a result, there was not a clear trail through the assessment stages to demonstrate that the projects awarded funding were those that had the greatest merit in terms of the published program guidelines ...

This shows that the recommendations made in the first audit, agreed by the department, had not been implemented by the department, and inadequate attention was given to relevant aspects of the grants administration framework. Effectively implementing agreed recommendations ... and closer adherence to identified principles of better practice grants administration are matters that warrant greater attention by the department ...

A further similarity between the third and fourth RDAF rounds and the first round was that a relatively high proportion of approved projects had not been recommended for approval by the panel ...

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4 ANAO, Audit Report No. 9 (2014-15), pp. 44-45. References to the 'published program guidelines' are to the department's 'RDAF Guidelines' published for rounds one to four. References to the 'grants framework' are to the framework in place at the time the funding rounds were completed (this included the *Financial Management and Accountability Act 1997* and the Commonwealth Grant Guidelines). Similar arrangements exist under the new framework, with the *Public Governance, Performance and Accountability Act 2013* and the Commonwealth Grants Rules and Guidelines taking effect from 1 July 2014. References to 'selection criteria' are to the four selection criteria for RDAF rounds three and four, as set out in Table 3.2, Audit Report No. 9, p. 69.

the then Government's guidelines for this program provided for the advisory panel to make the recommendations to the Minister as to those applications that should be awarded funding. Further, the grants administration framework has been designed to accommodate situations where decision-makers do not accept the advice they receive. Amongst other things, it requires that the basis for funding decisions be recorded. However, the records of the reasons for funding decisions taken contrary to panel advice generally provided little insight as to their basis and made no reference to the published selection criteria. This situation was particularly significant given that such decisions were largely at the expense of projects located in electorates held by the Coalition.<sup>5</sup>

- 2.8 The ANAO further noted that, in the context of improving grants administration, 'the most important message from this audit is that considerable work remains to be done to design and conduct regional grant programs in a way where funding is awarded, and can be seen to have been awarded, to those applications that demonstrate the greatest merit in terms of the published program guidelines'.<sup>6</sup>

## Audit recommendations and agency response

- 2.9 Table 2.2 sets out the recommendations for ANAO Report No. 9 and DIRD's response.<sup>7</sup>

Table 2.2 ANAO recommendations, Report No. 9 (2014-15)

1	<p>To improve the efficiency and effectiveness of any future two-stage grant application process, ANAO recommends that the Department of Infrastructure and Regional Development:</p> <ul style="list-style-type: none"> <li>• include an assessment of eligibility considerations as part of the design of the expression of interest stage so as to minimise the risk of ineligible applications being received and allow the second assessment stage to focus on merit considerations; and</li> <li>• minimise duplication of effort, and provide a clear line of sight through the assessment process, by drawing upon the results of the assessment of expressions of interest where there are similarities or inter-relationships between some of the shortlisting criteria for expressions of interest and the assessment criteria for full applications.</li> </ul> <p><b>DIRD's response:</b> <i>Agree.</i></p>
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5 ANAO, Audit Report No. 9 (2014-15), pp. 14-19. The response of the then Minister for Regional Services, Local Communities and Territories to the ANAO report and the ANAO comment is at Appendix 2, pp. 164-166. The RDAF advisory panel's response to the ANAO report and the ANAO comment is at Appendix 3, pp. 167-181.

6 ANAO, Audit Report No. 9 (2014-15), p. 21.

7 For details of DIRD's response to the ANAO's recommendations, see ANAO, Audit Report No. 9 (2014-15), pp. 159-161.

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2	<p>ANAO recommends that the Department of Infrastructure and Regional Development incorporate in the value with money methodology adopted in future granting activities an approach that reflects that applications assessed as not satisfactorily meeting the published merit assessment criteria are most unlikely to represent value with public money in terms of the objectives of the granting activity.</p> <p><b>DIRD's response:</b> <i>Noted.</i></p>
3	<p>To improve the quality and clarity of advice provided to decision-makers, ANAO recommends that in future advice on the merits of proposed grants where funding is to be allocated using a competitive merit-based selection process, the Department of Infrastructure and Regional Development provide advice that:</p> <ul style="list-style-type: none"> <li>• clearly and consistently establishes the comparative merit of applications relative to the program guidelines and merit criteria; and</li> <li>• includes a high level summary of the assessment results of each of the competing proposals in terms of their merit against the published criteria.</li> </ul> <p><b>DIRD's response:</b> <i>Agree.</i></p>

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## Committee review

- 2.10 Representatives from DIRD and the ANAO gave evidence at the Committee's public hearing on 6 March 2015.
- 2.11 As discussed below, the Committee focused on four matters regarding the ANAO report findings and evidence provided at the public hearing:
- Assessment and funding stages
  - Transparency and accountability
  - Implementation of ANAO report recommendations
  - Better practice regional grants administration

## Assessment and funding stages

- 2.12 By way of background, the assessment phase for RDAF funding involved the following stages:
- assessment of expressions of interest (EOIs) by 55 Regional Development Australia (RDA) committees, with projects being ranked in order of priority by region
  - assessment of eligible applications by DRALGAS, with those assessed as representing value with money being ranked in order of merit against the selection criteria overall
  - assessment of eligible applications by an advisory panel of five members selected for their experience, knowledge and expertise on

regional Australia (panel membership remained the same across each of the four RDAF rounds)<sup>8</sup>

- 2.13 The advisory panel's advice was provided to the then Minister for Regional Services, Local Communities and Territories by DRALGAS.<sup>9</sup> The results of the department's assessment of applications against the selection criteria were contained in 'assessment snapshots' and these were also provided to the Minister.<sup>10</sup>
- 2.14 As discussed below, the following matters were of interest concerning the RDAF assessment and funding stages: alignment of departmental and advisory panel assessment stages; the department's assessment of applications; the advisory panel's assessment of applications; and the Minister's funding decisions.

### Alignment of departmental and advisory panel assessment stages

- 2.15 The ANAO report noted that, similar to the first RDAF round and notwithstanding the department having agreed to a recommendation concerning this matter from the previous ANAO report, assessment of individual eligible applications against the published criteria, as recorded by the department and provided to the Minister for RDAF rounds three and four, did not align with the advisory panel's categorisation of applications.<sup>11</sup>
- 2.16 While the assessment and selection process, as described in the RDAF program guidelines, reflected a 'sound approach', the ANAO report therefore observed that in the manner implemented the stages were 'not well integrated in that each step informed the next in only a limited way'.<sup>12</sup> As the Auditor-General further commented:

A key conclusion of the audit was that there was not a clear trail through the various assessment stages adopted in rounds three and four to demonstrate that the projects recommended for funding, and those ultimately awarded funding, had the greatest merit in terms of the published selection criteria. In particular, the order of regional priority allocated to projects by the RDA committees was not used to inform the assessment of applications, and there was not a clear and consistent alignment between the

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8 ANAO, Audit Report No. 9 (2014-15), p. 103.

9 ANAO, Audit Report No. 9 (2014-15), p. 12.

10 ANAO, Audit Report No. 9 (2014-15), p. 110. Further explanation of this process was provided by Mr Gordon McCormick, General Manager, Regional Programs Branch, DIRD, *Committee Hansard*, Canberra, 6 March 2015, p. 3.

11 ANAO, Audit Report No. 9 (2014-15), p. 26.

12 ANAO, Audit Report No. 9 (2014-15), p. 14.

RDAF Advisory Panel's funding recommendations and the results of the department's assessment of each application against each of the published selection criteria.<sup>13</sup>

## Department's assessment of applications

2.17 The ANAO report observed that 'improvements in the quality of the department's assessment work were evident in the first RDAF round audited by ANAO' and this trend 'continued in the third and fourth funding rounds', particularly in relation to eligibility checking and conduct of risk assessments.<sup>14</sup> However, the ANAO noted 'significant shortcomings in the methodology' used by the department to assess the merit of competing applications in terms of the published selection criteria and that the department had not fully implemented previous ANAO report recommendations concerning the first RDAF funding round 'designed to address these shortcomings'.<sup>15</sup> As the ANAO commented, 'instead of fully implementing these recommendations', the department retained:

- the same qualitative rating scale it had used in the first funding round, notwithstanding that it 'does not provide a clear and consistent basis for effectively discriminating between the relative merits of competing applications'
- an 'unsound methodology' for assessing value with public money, whereby applications assessed as not satisfactorily meeting up to three of the four selection criteria were identified as representing value with money<sup>16</sup>

## Advisory panel's assessment of applications

2.18 The RDAF advisory panel was tasked with considering the individual and relative merits of 192 eligible applications in round three, and 159 eligible applications in round four, and with recommending the most meritorious to the Minister.<sup>17</sup> As required by the program guidelines, the advisory panel classified each eligible application into one of three categories:

- Recommended for Funding (RFF)

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13 Mr McPhee, Auditor-General, ANAO, 'Opening statement', *Submission 2*, p. 2.

14 ANAO, Audit Report No. 9 (2014-15), p. 22.

15 ANAO, Audit Report No. 9 (2014-15), p. 22. (See ANAO recommendations 1-3, Audit Report No. 3 (2012-13), pp. 28-29.) Implementation of the ANAO report recommendations and DIRD's comments on this matter are further discussed in a later section.

16 ANAO, Audit Report No. 9 (2014-15), p. 22. As the ANAO noted, 'applications that do not satisfactorily meet each of the published selection criteria are most unlikely to represent value with public money in terms of the objectives of the granting activity', p. 22.

17 ANAO, Audit Report No. 9 (2014-15), pp. 22-23.

- Suitable for Funding (SFF)
- Not Recommended for Funding (NRF)<sup>18</sup>

2.19 The ANAO report found that, while the advisory panel viewed those projects it recommended as being of the highest quality, the approach the panel adopted to determining its recommendations was 'not consistent with a transparent, competitive, merit-based process to awarding grant funding in accordance with an assessment of applications against the published criteria'.<sup>19</sup> As the ANAO further explained, notwithstanding the recommendations of the previous ANAO report on the first RDAF round, 'the methodology the panel had developed in August 2011 on the first day of its deliberations for the first funding round continued to be applied in May 2013 for rounds three and four'.<sup>20</sup> As a result, and notwithstanding that the program guidelines required the advisory panel to assess and rank eligible applications based on the published selection criteria, there were 'no documented panel assessments of each application in relation to those criteria'.<sup>21</sup> As the Auditor-General further commented:

While the ANAO has no fundamental issue with the Advisory Panel reaching a different view to the department as to the individual or relative merits of applications, at issue is that the panel did not then document an assessment of each application against each selection criterion to support or explain its recommendations. This approach, combined with the panel's meeting minutes not otherwise adequately outlining the rationale for decisions taken, means that the demotion of some projects and promotion of others compared with the only recorded ratings awarded against the selection criteria (being the department's) was unexplained.<sup>22</sup>

2.20 There was interest in further understanding the categorisation of applications by the advisory panel – in particular, how the final overall scoring out of 50 for each application supported the categories of RFF, SFF and NRF.<sup>23</sup> The ANAO provided a detailed description of this process at the public hearing.<sup>24</sup> As the ANAO then summarised, 'the panel, as they

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18 ANAO, Audit Report No. 9 (2014-15), p. 12.

19 ANAO, Audit Report No. 9 (2014-15), p. 24.

20 ANAO, Audit Report No. 9 (2014-15), p. 23.

21 ANAO, Audit Report No. 9 (2014-15), p. 23.

22 Mr McPhee, ANAO, 'Opening statement', *Submission 2*, p. 2.

23 For further detail on this aspect of the advisory panel's assessment approach, see ANAO, Audit Report No. 9 (2014-15), p. 91.

24 Mr Brian Boyd, Executive Director, ANAO, *Committee Hansard*, Canberra, 6 March 2015, pp. 2-3.



put it, assessed each application in its entirety and gave the entire application therefore a score and then added their individual scores together and compared them', but the 'problem' with that is it 'does not give you an insight into whether an application was seen as less worthy because its partnership funding was no good or its regional benefits were not as great'.<sup>25</sup> The department completed an individual assessment of each eligible application against each individual selection criterion and 'the panel, in its own words, challenged and re-rated that'.<sup>26</sup> However, while the ANAO agreed that that was a 'sound and good process; that is why you have a panel', the 'criticism' the ANAO had of the panel was that 'they did not then update those individual criterion assessments to reflect their views so that both we, looking in, and the minister could have the benefit of seeing that, and also unsuccessful applicants would have been able to be told, ultimately: "This is why you were unsuccessful. It was because you performed poorly here but well there"'.<sup>27</sup>

2.21 In terms of the differing views of the advisory panel concerning a number of matters relating to the ANAO audit,<sup>28</sup> Mr Boyd, Executive Director, ANAO, further explained the ANAO's findings:

[the panel] are referring there to the issue ... about the notion as to whether it is adequate in the grants administration framework for them to conduct an overall assessment and come to an overall view against each application without supporting that, recording their assessment of each application in terms of each criterion. From our perspective, I guess we have a somewhat different view to the panel as well – and I think theirs is hard to support – as to what extent they have to operate in accordance with that grants administration framework. They argue in, I think, their first substantive point that they do not need to operate in accordance with that, because they are outside of it. I think we clearly point out that is not the case. I do not think the department disagrees with us ... The Commonwealth Grant Guidelines have been updated twice, and now they are the Commonwealth Grant Rules and Guidelines. The guidance to external panels in that has been made even more clear, because there has been some confusion for some panels about whether they have to do things in accordance with the framework. So the Department of Finance has made that

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25 Mr Boyd, ANAO, *Committee Hansard*, Canberra, 6 March 2015, pp. 5-6.

26 Mr Boyd, ANAO, *Committee Hansard*, Canberra, 6 March 2015, p. 6.

27 Mr Boyd, ANAO, *Committee Hansard*, Canberra, 6 March 2015, p. 6.

28 For the advisory panel's response to the ANAO report, together with the ANAO comment, see Appendix 3, 'Former RDAF Advisory Panel's response', Audit Report No. 9 (2014-15), pp. 167-181.

abundantly clear, and one of the things that are a requirement is that the merit advice to ministers address the selection criteria ...

We have said, 'The department has done an assessment against each criterion to inform your work.' In their own words to us, they challenged and re-rated some of those, and we think that is a good and sound process. That is why they are employed. They are not employed just to tick what the department has done; there would be no point having them. But, in doing so, all they did was come up with different overall conclusions without explaining which of the criteria the department got it wrong on.<sup>29</sup>

## Minister's funding decisions

2.22 The ANAO report highlighted a number of matters regarding the ministerial advice provided by the department and the advisory panel for RDAF rounds three and four.<sup>30</sup> The ANAO concluded that the 'approach taken to advising the Minister as to which round three and four applications should be awarded funding had a number of significant shortcomings':

- applications were banded into a small number of categories, which offered the Minister limited assistance in terms of delineating the relative merits of competing applications;
- the briefing materials were voluminous, with insufficient summary material provided by the department. Such an approach makes it difficult for any decision-maker to compare the assessed merits of competing applications; and
- similar to the first round and notwithstanding the department agreeing to an ANAO recommendation that it enhance the documentation provided to the Minister to ensure assessment outcomes aligned with funding recommendations, the assessment of individual eligible applications against the published criteria (as recorded by the department and provided to the Minister) did not align with the panel's categorisation of applications.<sup>31</sup>

2.23 By way of background, the ANAO report found that, by ranking large numbers of applications equally by grouping them into a small number of bands, the advisory panel's approach 'represented a marked decline in the

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29 Mr Boyd, ANAO, *Committee Hansard*, Canberra, 6 March 2015, pp. 13-14.

30 For the advisory panel's response to the ANAO report, together with the ANAO comment, see Appendix 3, 'Former RDAF Advisory Panel's response', Audit Report No. 9 (2014-15), pp. 167-181. Implementation of the ANAO report recommendations for the first RDAF funding round and DIRD's comments on this matter are further discussed in a later section.

31 ANAO, Audit Report No. 9 (2014-15), p. 26.

degree of differentiation offered to the Minister compared to the first funding round':

For rounds three and four, the extent to which the Minister did not approve applications categorised by the panel as RFF was considerably higher than round one but the Minister did not have the benefit of applications in the SFF category being individually ranked so that it was not possible for her to work through those applications in the manner that had occurred in round one.<sup>32</sup>

- 2.24 The ANAO report also found that the round three and four briefing packages sent by the department to the then Minister did not contain a summary table – '[i]n the absence of summary information, the advice provided on how each RDAF application had been assessed against the selection criteria was not in a format that would have enabled the Minister to readily form her own conclusion as to how an individual application performed relative to competing applications'.<sup>33</sup> As the ANAO further explained, the results of the department's assessment were contained in 'assessment snapshots' – these were 'sent separately in hard copy format within multiple folders, with the Minister being sent 192 one-page assessment snapshots for round three, and 159 assessment snapshots averaging six pages each for round four'.<sup>34</sup> Exacerbating the situation was the fact that, according to the ANAO, the department 'made too many errors in the assessment snapshots'.<sup>35</sup>
- 2.25 The ANAO further noted the constrained assessment time frames available to the department and the advisory panel in rounds three and four – 'the department's response back to us, quite fairly, points to the fact that they had less time to check things and get it right ... it would be wrong for us not to at least emphasise that to the committee. It does not excuse things, but ... it helps put things in a bit of context as well'.<sup>36</sup> DIRD confirmed that, while 'additional time would allow some greater quality assurance and reduce that particular risk ... we did not say that we could not do it at the right quality in the new time frames set'.<sup>37</sup>
- 2.26 As the ANAO observed at the public hearing, 'there were a number of issues. Some of them would not have been visible, but the fact is that

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32 ANAO, Audit Report No. 9 (2014-15), p. 23.

33 ANAO, Audit Report No. 9 (2014-15), p. 110.

34 ANAO, Audit Report No. 9 (2014-15), p. 110.

35 Mr Boyd, ANAO, *Committee Hansard*, Canberra, 6 March 2015, p. 5.

36 Mr Boyd, ANAO, *Committee Hansard*, Canberra, 6 March 2015, pp. 9-10. Mr Boyd also commented on some of things that the department recorded at the time as 'actions to undertake in light of reduced time frame', p. 10.

37 Ms Lyn O'Connell, Deputy Secretary, DIRD, *Committee Hansard*, Canberra, 6 March 2015, p. 10.

ministers, from our perspective, should be able to rely upon departments and panels getting that right for them'.<sup>38</sup>

2.27 As well as a lack of alignment between departmental and advisory panel assessment stages for RDAF rounds three and four, the ANAO report pointed to a lack of alignment between assessment and funding stages:

A feature of the round three and round four decision-making was the lack of alignment with the assessment advice provided to inform those decisions. It is difficult to see such a result as being consistent with the competitive merit-based selection process outlined in the published program guidelines:

- only 53 (44 per cent) of the 121 approved applications had been assessed by the department as satisfying each of the published selection criteria. Further, among those applications not approved were 79 applications seeking a total of \$292 million that had been assessed as satisfying each selection criterion and as representing value with public money; and
- nearly half of the funding awarded (48 per cent) went to applications that had not been recommended by the panel and a third of recommended applications were not approved.

Specifically, the Minister:

- ⇒ rejected 41 projects that had been recommended for funding of \$93 million; and
- ⇒ approved \$109 million in funding for 33 projects that had not been recommended by the panel.<sup>39</sup>

2.28 It is noted that a third of the applications awarded the highest possible rating against each selection criteria by the department were assigned to the lowest merit category by the panel.<sup>40</sup>

2.29 As the Auditor-General further observed:

The then Minister approved 88 of the 129 applications that had been recommended for funding by the panel across rounds three and four, and so rejected the other 41 applications. In addition, the then Minister approved 33 applications that had not been recommended for funding, of which 10 had been categorised as 'Suitable for Funding' and 23 had been categorised as 'Not Recommended for Funding' by the panel. Therefore, 27 per cent of the applications approved (representing 48 per cent of the \$226 million awarded) had not been recommended for funding by the panel.<sup>41</sup>

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38 Mr Boyd, ANAO, *Committee Hansard*, Canberra, 6 March 2015, p. 6.

39 ANAO, Audit Report No. 9 (2014-15), p. 27.

40 ANAO, Audit Report No. 9 (2014-15), p. 15.

41 Mr McPhee, ANAO, 'Opening statement', *Submission 2*, p. 3.

- 2.30 The Auditor-General emphasised the broader point that ‘when you look ... at ... the minister’s funding decisions, you can see that the minister is approving applications from not only the SFF ... but also from the NRF as well. So, ours is a broader point ... The minister was recommended by the panel to just go with the top level. For whatever reason, she has moved more broadly into the full range of categories, just not the SFF categories’.<sup>42</sup>
- 2.31 A related issue that emerged here concerned a difference in opinion as to whether or not RDAF projects classified as ‘Suitable for Funding’ were available for selection by the Minister, and whether or not the Minister therefore had to report to the Finance Minister approval of any grant application from this category.<sup>43</sup> As the ANAO report explained:
- In each of the four rounds, the panel recommended that funding be approved only for those applications it had included in the ‘Recommended for Funding’ category ... However, the Minister has informed the ANAO that: she had been advised by the department, and was always of the understanding, that projects in both the ‘Recommended for Funding’ and ‘Suitable for Funding’ categories were available for selection; in choosing projects from both categories she was complying with the program guidelines; and she would have reported to the Finance Minister her decisions to award funding to an application included in the ‘Suitable for Funding’ category if she had believed that the panel had not recommended them for funding.<sup>44</sup>
- 2.32 The ANAO noted that they and the department held different perspectives on whether there was a requirement for the Minister to report to the Finance Minister on RDAF funding applications approved from the SFF category: ‘[o]ur perspective was that they did, and it was the same perspective we had in round 1. The department ... has held the same perspective throughout as well: it does not consider that they require reporting to the finance minister’.<sup>45</sup> As DIRD confirmed, ‘[o]ur view ... was that those projects that were not recommended for funding needed to be advised ... we did not advise that those that were suitable for funding and selected by the minister needed to be advised ... So the difference here is between the ANAO’s view of the guidelines and ours. We recommended to the minister that she advise the Minister for Finance only

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42 Mr McPhee, ANAO, *Committee Hansard*, Canberra, 6 March 2015, p. 8. See also Mr Boyd, ANAO, on this point, p. 9.

43 In the context of the grants administration framework there is an ‘obligation to report to the Finance Minister instances where a Minister approves ... any applications that were recommended for rejection’ – see ANAO, *Audit Report No. 9 (2014-15)*, p. 134.

44 ANAO, *Audit Report No. 9 (2014-15)*, p. 17. See the response of the then Minister to the ANAO report and the ANAO comment at Appendix 2, pp. 164-166.

45 Mr Boyd, ANAO, *Committee Hansard*, Canberra, 6 March 2015, p. 12.

where they were not recommended'.<sup>46</sup> The public hearing further explored this difference in viewpoint concerning whether or not RDAF projects classified as 'SFF' were available for selection by the Minister, and whether or not the Minister therefore had to report to the Finance Minister approval of any grant application from this category – this discussion is cited in full at Figure 2.1.

- 2.33 In terms of documenting grant funding decisions, the ANAO report observed that the 'grants administration framework has been designed to accommodate situations where decision-makers do not accept the advice they receive. Amongst other things, it requires that the basis for funding decisions be recorded'.<sup>47</sup> As the Auditor-General stated, '[w]hile it is open to a Minister to reach a decision different from that recommended by a panel or department, it is important that the rationale for such decisions be documented and be consistent with the published program guidelines and with any other applicable Commonwealth policies and legislation'.<sup>48</sup> However, the Auditor-General noted that, 'where the then Minister's funding decisions diverged from the panel's recommendations in rounds three and four, the recorded reasons did not refer explicitly to the published selection criteria and generally provided little insight'.<sup>49</sup> As the ANAO report observed, the records instead 'tended toward generalised statements'.<sup>50</sup> At the public hearing, the ANAO provided examples of such statements,<sup>51</sup> and further noted that:

the [ANAO] report recognises ... that ministers have that discretion to make decisions which differ from the recommendations ... one of the key things we looked to, in accordance with the grants administration framework, is that ministers adequately record their reasons for decisions ... The challenge here is that in a small number of instances ... no reason was recorded. In others the reason was often the same reason repeated again and again, often 'not sufficient regional benefit'. In terms of the selection criteria, from our perspective, that provides little insight as to why some projects that were recommended are being moved past.<sup>52</sup>

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46 Ms O'Connell, DIRD, *Committee Hansard*, Canberra, 6 March 2015, pp. 12-13.

47 ANAO, Audit Report No. 9 (2014-15), p. 18.

48 Mr McPhee, ANAO, 'Opening statement', *Submission 2*, p. 3.

49 Mr McPhee, ANAO, 'Opening statement', *Submission 2*, p. 3.

50 ANAO, Audit Report No. 9 (2014-15), p. 28.

51 Mr Boyd, ANAO, *Committee Hansard*, Canberra, 6 March 2015, pp. 11-12.

52 Mr Boyd, ANAO, *Committee Hansard*, Canberra, 6 March 2015, p. 7, p. 9.

Figure 2.1 *Committee Hansard, Canberra, 6 March 2015, pp. 7-8 (Mr Pat Conroy MP, Deputy Chair, JCPAA; Mr Brian Boyd, ANAO; and Ms Lyn O'Connell, DIRD)*

**Mr CONROY:** ... It seems to be very clear in the audit process that the department at the time considered 'suitable for funding' as consistent with the guidelines. I would like to draw everyone's attention to the guidelines for RDAF round 4 ...

The panel may choose to consider the distribution of funding of projects rated 'recommended for funding' or 'suitable for funding' in its recommendations to the minister ... page 137 of the [ANAO] report on the same issue ... details how the department provided advice to the minister around notification to the Minister for Finance for projects that she had approved, but that were not recommended. It is true to say that ... advice ... does not recommend that the minister must notify the Department of Finance when she approved projects that were classified 'suitable for funding'.

**Ms O'Connell:** My understanding is that it was restricted to the not-suitable-for-funding category, which is what we understand to be the right practice.

**Mr CONROY:** So we have clear guidelines that say that the panel can recommend projects ranked 'suitable for funding'. We have clear advice from the department to the minister that she does not need to notify the Minister for Finance when she approves projects that are classified 'suitable for funding'. Mr Boyd, is it true that you are siding with the panel's assessment, but it seems that the minister had very clear advice from the department and had guidelines to rely on that suitable-for-funding projects were projects she could approve?

**Mr Boyd:** I would not agree with that. Rather than having me talking in the abstract on this, I might read into the record the actual advice that the minister received. Yes, the guidelines did allow that capacity for the panel or the department to recommend that the minister approve not only those in the RFF top bucket, but also the suitable-for-funding second bucket. But that is not what happened. This is from the opening paragraph of the round 3 brief; I will then read the opening paragraph from the round 4 brief, which contains the recommendation:

The Chair has written to you recommending that 95 projects be funded at a cost of up to \$38.59 million.

Those are the ones in the RFF category. There was no recommendation that she also fund the SFF. Similarly the opening paragraph of the round 4 brief – the key recommendation – says:

The Chair has written to you recommending that 34 projects be funded at a cost of up to \$172,474,143.

It refers to an attachment A. Attachment A is an attachment to the panel's letter, which lists each of those projects. Again, those projects, which are described as a list of projects recommended by the panel for funding, are only those in the recommended for funding bucket. So, yes, the guidelines provided that capacity, and ... the panel considered distribution in coming to its recommendations ... But then the panel came to the considered view, as clearly expressed in both briefs, that the only projects they are recommending for funding are those in the recommended for funding bracket.

**Mr CONROY:** Mr Boyd, what I am focused on here is, firstly, that the guidelines clearly imply that both categories are able for approval by the minister and, secondly, the clear advice from the department, as confirmed by testimony just given by Ms O'Connell that she does not have to notify the Minister for Finance when she approves projects considered suitable for funding, which would seem to imply that the minister considered, on departmental advice, that she was acting consistently with the grant guidelines ...

... my broader point is that we have already established, through the report and the testimony, that the panel and the department's assessment of who fitted into those categories was incredibly flawed. So the minister's selection of projects outside that was fine. Additionally, the current minister has confirmed that assessment by continuing with those projects that were not recommended by the panel.

2.34 As the Auditor-General concluded, '[w]e do not have a problem with different steps and stages taking a different view. In fact, we fully expect that to happen ... Our only point is that the process should be quite clear about each responsible area making the call, but being clear as to the basis for the decision ... we are respectful of the different views that different parts of the process may have along the way; but please be accountable for the calls that you make and document them'.<sup>53</sup>

2.35 There was interest in further exploring the RDAF arrangements following the change of government<sup>54</sup> on the basis that the current Minister had continued to fund all the projects in rounds three and four that the previous Minister had determined to fund – in particular, concerning the information that the current Minister had received from the department on these projects and whether in fact it would be unusual for a new incoming government to withdraw grant funding from applicants who had already been notified that they were successful. DIRD confirmed that '[a]ll grants for rounds 3 and 4 were continued and funded'.<sup>55</sup> DIRD further confirmed that this included 'dozens and dozens' of grants that were uncontracted when change of Government occurred.<sup>56</sup> DIRD also explained that:

... we provided the current government with a list of projects that were successful and unsuccessful – not the information and briefings we provided to the minister of the previous government but the end outcomes of successful and unsuccessful grant applicants – and the recommendations of the panel as well in order to inform the government's decision making about whether they would proceed with funding those grants or not ... as part of aiding their decision-making process, we provided information on our assessment of the project, the panel's view and what was funded and not funded ...

There was a decision point with the change of government as to whether they would continue to fund them or not, particularly where they were not yet contracted. Where they were contracted, they were continuing. That was a commitment of the current government as it came to government. But this was to aid decision making about those not contracted grants ...

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53 Mr McPhee, ANAO, *Committee Hansard*, Canberra, 6 March 2015, p. 14.

54 By way of background, at the time of the change of government in September 2013, '57 of the projects approved in rounds two to four of RDAF did not have a signed funding agreement', ANAO, Audit Report No. 9 (2014-15), p. 39.

55 Ms O'Connell, DIRD, *Committee Hansard*, Canberra, 6 March 2015, p. 5.

56 Mr McCormick, DIRD, *Committee Hansard*, Canberra, 6 March 2015, p. 14, p. 24.



The government of the day chose to go ahead with contracting rounds 3 and 4 contract[s] where they had not yet been contracted. The government of the day chose not to proceed with any of the round 5 contracts. No discussions had been held about those contracts with the proponents.<sup>57</sup>

We provide advice, a brief, to the minister with a recommendation to fund or not to fund, based on the value-for-money assessment.<sup>58</sup>

- 2.36 It is noted that successful recipients of round five RDAF grants had been notified.

## Transparency and accountability

- 2.37 The ANAO report concluded that, '[i]n a number of important respects, the conduct of the third and fourth RDAF funding rounds was not consistent with the accountability and transparency principles outlined in the grants administration framework' – and of 'particular note' here was that the recording of reasons for funding decisions 'did not adequately explain how the preference evident for projects located in Australian Labor Party (ALP)-held electorates had resulted from a merit-based process. In particular, those projects had a much higher approval rate than those located in Coalition-held electorates'.<sup>59</sup>
- 2.38 As the Auditor-General noted, 'where the then Minister's funding decisions diverged from the panel's recommendations in rounds three and four, the recorded reasons did not refer explicitly to the published selection criteria and generally provided little insight. This situation was particularly significant given that such decisions were largely at the expense of projects located in electorates held by the Coalition'.<sup>60</sup>
- 2.39 The Committee noted that 10 out of 23 projects rated 'Not Recommended for Funding' subsequently selected for funding were located in non-Labor held seats (including four Coalition and five Independent).<sup>61</sup>
- 2.40 The ANAO confirmed that it was 'quite common' for relevant ANAO reports to consider the electoral distribution of funding,<sup>62</sup> and that the ANAO Better Practice Guide on *Implementing Better Practice Grants*

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57 Ms O'Connell, DIRD, *Committee Hansard*, Canberra, 6 March 2015, p. 4, p. 24.

58 Mr McCormick, DIRD, *Committee Hansard*, Canberra, 6 March 2015, p. 14.

59 ANAO, Audit Report No. 9 (2014-15), p. 29.

60 Mr McPhee, ANAO, 'Opening statement', *Submission 2*, p. 3. See the response of the then Minister to the ANAO report and the ANAO comment at Appendix 2, pp. 164-166.

61 Mr Boyd, ANAO, *Committee Hansard*, Canberra, 6 March 2015, p. 20. See also ANAO, Audit Report No. 9 (2014-15), p. 128.

62 Mr McPhee, ANAO, *Committee Hansard*, Canberra, 6 March 2015, p. 19. The ANAO pointed to a number of audit reports that had included this information – see *Submission 2.1*, p. 2.

*Administration*<sup>63</sup> and Commonwealth Grants Rules and Guidelines also make reference to analysis of electoral distribution as a measure to evaluate the equity of a program:

The ANAO has observed that, in its performance audits of grant programmes, it has put an emphasis on the geographic distribution of certain grant programmes as a measure of equitable distribution and as an indicator of party-political bias in the distribution of grants. The ANAO has emphasised that those involved in grants administration should therefore be aware that the geographic and political distribution of grants may be seen as indicators of the general equity of a programme.<sup>64</sup>

- 2.41 It was pointed out that the distribution by political party of total funding approved for RDAF rounds one to four was 46 per cent for the Australian Labor Party and 46 per cent for the Coalition, with Coalition seats receiving \$4.5 million more than ALP seats across the four funding rounds.<sup>65</sup> However, the ANAO report noted that ‘while electorates held by the two major parties were awarded an equal portion of the \$575.8 million approved in total across the four funding rounds (being 46 per cent each), this result did not align with the distribution of funding requested or recommended’; rather, ‘projects located in Coalition-held electorates had represented both the majority of the RDAF funding requested (55 per cent) and the majority of the funding recommended (59 per cent) but were less successful in being awarded funding (46 per cent)’.<sup>66</sup>
- 2.42 The ANAO’s use of an Australian Electoral Commission (AEC) classification of electorates as ‘rural or provincial’ was further discussed at the public hearing.<sup>67</sup> (The ANAO report had made reference to one of its findings as being ‘consistent with the extent to which the Coalition held electorates defined by the Australian Electoral Commission as rural or provincial’.<sup>68</sup>)

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63 See ANAO, *Implementing Better Practice Grants Administration*, Better Practice Guide, December 2013, p. 94 – quoted in ANAO, *Submission 2.1*, pp. 2-3.

64 *Commonwealth Grants Rules and Guidelines*, Department of Finance, July 2014, paragraph 13.9, p. 35 – quoted in ANAO, *Submission 2.1*, p. 3.

65 See ANAO, Table 6.2, ‘Distribution by political party of total funding approved under rounds one to four’, Audit Report No. 9 (2014-15), p. 151.

66 ANAO, Audit Report No. 9 (2014-15), pp. 150-151.

67 See Mr Boyd, ANAO, *Committee Hansard*, Canberra, 6 March 2015, pp. 19-22; and Mr McCormick, DIRD, *Committee Hansard*, Canberra, 6 March 2015, pp. 20-21. DIRD provided further details about the applications received in RDAF round four, including how many were identified as having a project located in a capital city, as well as details of the key points of difference between the program guidelines for rounds three and four – see *Submission 1.2*, pp. 1-2.

68 ANAO, Audit Report No. 9 (2014-15), pp. 150-151.

- 2.43 By way of background, the purpose of RDAF round three was to ‘support projects in towns with a population of 30 000 people or less’, while round four ‘sought to support strategic infrastructure projects, which could be located in any Australian town or city’.<sup>69</sup> The program guidelines for round four further advised that ‘projects located in a capital city must demonstrate how the project will benefit the broader region’ – however, there was ‘no requirement that regional Australia be a beneficiary of the projects located in capital cities’.<sup>70</sup>
- 2.44 ANAO reference to the AEC classification of electorates as ‘rural or provincial’ was therefore queried on the basis that, firstly, a number of electorates classified by the AEC as ‘outer metropolitan’ – and so excluded from the ‘rural or provincial’ classification – also take in regional towns (a range of electorates containing regional communities do not align precisely with the AEC’s definition of ‘rural or provincial’ electorates); and, secondly, RDAF funded some projects in urban areas to the benefit of the broader region, rather than regional Australia specifically.
- 2.45 On another matter, DIRD was asked if it was standard practice for information to be publicly disclosed about whether grant applications not approved by a minister had been recommended by a panel or department and, alternatively, about whether grant applications approved by a minister had not been recommended by a panel or department. Ms Lyn O’Connell, Deputy Secretary, DIRD, responded that ‘[m]y observation of practice is that it is not common for such information to be made public’.<sup>71</sup> As DIRD further explained, ‘[w]hen grant decisions are made it is common practice that the minister will make public the successful recipients. Usually there is a letter to the unsuccessful applicants. But it is not common practice that either the department or necessarily the minister would make public the list of unsuccessful grant applicants’.<sup>72</sup>
- 2.46 There was also interest in who, beyond the department, might have received information about projects recommended but not approved and projects approved but not recommended.<sup>73</sup> DIRD confirmed that, in addition to the department and the then Minister, the panel members and the incoming Assistant Minister for Infrastructure and Regional Development received this information.<sup>74</sup>

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69 ANAO, Audit Report No. 9 (2014-15), p. 41, p. 43.

70 ANAO, Audit Report No. 9 (2014-15), p. 66, p. 67.

71 Ms O’Connell, DIRD, *Committee Hansard*, Canberra, 6 March 2015, p. 4.

72 Ms O’Connell, DIRD, *Committee Hansard*, Canberra, 6 March 2015, p. 4.

73 DIRD provided further explanation on this point – see Ms O’Connell, DIRD, *Committee Hansard*, Canberra, 6 March 2015, pp. 4-5.

74 Ms O’Connell, DIRD, *Committee Hansard*, Canberra, 6 March 2015, p. 4.

## Implementation of ANAO report recommendations

- 2.47 The ANAO conducted a previous audit of the design and conduct of RDAF round one in September 2012, making three recommendations, as set out in Table 2.3.<sup>75</sup>
- 2.48 There was interest in how the department had implemented these previous recommendations. The ANAO report observed that the department had 'agreed to all three recommendations' from this previous audit and noted it would 'adopt the recommendations in round three and subsequent funding rounds'.<sup>76</sup> However, the ANAO concluded that:

The absence of alignment or a clear trail between the assessed merit of applications against the published selection criteria and the rounds three and four funding decisions was a similar situation to that observed in ANAO's audit of the first RDAF funding round. This shows that the recommendations made in the first audit, agreed by the department, had not been implemented by the department ... Effectively implementing agreed recommendations (which often reflect ANAO's experience of practices other departments have found to be beneficial) and closer adherence to identified principles of better practice grants administration are matters that warrant greater attention by the department.<sup>77</sup>

Table 2.3 ANAO recommendations, Report No. 3 (2012-13)

1	To provide a more efficient and effective means of differentiating between eligible applications in terms of their overall claims against the published assessment criteria, ANAO recommends that the Department of Regional Australia, Local Government, Arts and Sport, in consultation with the Regional Development Australia Fund advisory panel, adopt a numerical rating scale for the merit assessment stage of future funding rounds. <b>Regional Australia response:</b> <i>Agree.</i>
2	In designing and administering grant programs, ANAO recommends that the Department of Regional Australia, Local Government, Arts and Sport clearly outline to decision-makers the basis on which it has been assessed whether each application represents value for money in the context of the published program guidelines and program objectives. <b>Regional Australia response:</b> <i>Agree.</i>
3	ANAo recommends that, consistent with the key principles for grants administration outlined in the Commonwealth Grant Guidelines, the Department of Regional Australia, Local Government, Arts and Sport improve the documentation provided to the Minister in respect to the assessment of individual eligible applications against the published criteria to promote a clear alignment between these assessments and the order of merit for funding recommendations. <b>Regional Australia response:</b> <i>Agree.</i>

75 ANAO, Audit Report No. 3 (2012-13), *Design and Conduct of the First Application Round for the Regional Development Australia Fund*, DRALGAS, pp. 28-29.

76 ANAO, Audit Report No. 9 (2014-15), p. 40.

77 ANAO, Audit Report No. 9 (2014-15), p. 16.

- 2.49 By way of background, ‘instead of fully implementing these recommendations’, the ANAO found that the department had retained the ‘same qualitative rating scale it had used in the first funding round’ and an ‘unsound methodology for assessing value with public money’.<sup>78</sup> Further, ‘notwithstanding the department agreeing to an ANAO recommendation that it enhance the documentation provided to the Minister to ensure assessment outcomes aligned with funding recommendations’, the assessment of individual eligible applications against the published criteria, as recorded by the department and provided to the Minister, ‘did not align with the panel’s categorisation of applications’.<sup>79</sup>
- 2.50 However, DIRD considered that it had implemented these recommendations: ‘[w]hile the ANAO report for Rounds Three and Four indicated that, in their view, the recommendations from Round One had not been implemented, the Department disagrees and considers that it has implemented the recommendations’.<sup>80</sup> At the public hearing, DIRD provided further details on how it had implemented these recommendations.<sup>81</sup>
- 2.51 There was also interest in DIRD’s progress in implementing the ANAO recommendations from the current audit report, for RDAF rounds three and four. The department provided an update on its implementation of these recommendations.<sup>82</sup>

## Better practice regional grants administration

- 2.52 The ANAO report concluded that, in the context of improving grants administration, the ‘most important message’ from its audit of RDAF rounds three and four is that ‘considerable work remains to be done to design and conduct regional grant programs in a way where funding is awarded, and can be seen to have been awarded, to those applications that demonstrate the greatest merit in terms of the published program guidelines’.<sup>83</sup>
- 2.53 As the ANAO further noted, while performance audits have been undertaken of ‘each of the major regional grant funding programs introduced by successive governments over the last eleven years’ and

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78 ANAO, Audit Report No. 9 (2014-15), p. 22.

79 ANAO, Audit Report No. 9 (2014-15), p. 26.

80 DIRD, *Submission 1*, p. 1.

81 Ms O’Connell, DIRD, *Committee Hansard*, Canberra, 6 March 2015, p. 2. For further details on this matter, see also DIRD, *Submission 1*, pp. 2-3.

82 See Ms O’Connell, DIRD, *Committee Hansard*, Canberra, 6 March 2015, p. 1.

83 ANAO, Audit Report No. 9 (2014-15), p. 21.

‘improvements have been observed in some important aspects of the design and implementation of regional grant programs’ over this period, for each successive program there have been ‘shortcomings in the design and administration of the assessment and decision-making processes, and indicators of bias in the awarding of funding to government-held electorates’.<sup>84</sup>

- 2.54 Accordingly, there was interest in how regional grants program administration might be improved in the future. As the JCPAA Chair observed:

These sorts of programs have been prone to these sorts of problems. How do we do better? We have talked about the better practice guide. We have had numerous recommendations, and you have outlined them in your report, and the recommendations have all been agreed. But we keep coming back to this point ... You could probably have a stack of Audit Office reports on regional programs, but how do we get it right?<sup>85</sup>

- 2.55 The Auditor-General concluded by emphasising the ‘long-term gain’ from such audit processes over time and the importance of ministers calling for good practice from their departments:

Our work is really, genuinely designed to stimulate better administration in the long term. There is a bit of short-term pain, but there is long-term gain from these audit processes and the responses by the department. I think the reason we issue the better practice guide is to try and bring together all of our collective experience, which draws off agencies’ experiences as well, and put it out there. I think, though, there is nothing more important than the ministers saying to their departments, ‘I want a good practice process here.’ There are risks when timetables get shortened. We see it more broadly in public administration. When agencies operate under time pressures the risks do go up. But it is up to agencies to manage those risks or to inform government, if they cannot, what other options might be available ... with the committee’s support, our continuing work and the positive and constructive responses from departments, we will get a better outcome, an outcome that still is respectful of the roles of the different parties in the process and, at the end of the day, of the responsibilities of ministers to make decisions.<sup>86</sup>

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84 ANAO, Audit Report No. 9 (2014-15), pp. 19-20.

85 Dr Southcott MP, Chair, JCPAA, *Committee Hansard*, Canberra, 6 March 2015, p. 23.

86 Mr McPhee, ANAO, *Committee Hansard*, Canberra, 6 March 2015, p. 23.

- 2.56 Against this background, there was also interest in the broader design of the current regional grants program being administered by DIRD, the National Stronger Regions Fund (NSRF),<sup>87</sup> as well as how the department was implementing ANAO recommendations from current and past audits in terms of this new program. DIRD provided further details about this matter,<sup>88</sup> and confirmed that, in designing the NSRF, ‘we have had regard to the ANAO’s findings in relation to all of its audits on regional programs, particularly its latest audit on rounds 3 and 4. We believe we have taken into account the ANAO’s recommendations and adjusted the way that program will operate accordingly’.<sup>89</sup>
- 2.57 DIRD explained that it was currently going through the process of assessing submissions for round one of NSRF and that it would then ‘provide advice to the ministerial panel, which in consultation with the government will make decisions on which applications they will fund’.<sup>90</sup> DIRD also confirmed that there would be ‘further rounds’ of funding for the NSRF and therefore ‘some flexibility’ in how much money there would be for the first round.<sup>91</sup> The ANAO made some initial observations on these matters in terms of the design and funding of the NSRF.<sup>92</sup>
- 2.58 It was noted that the design and implementation of NSRF was listed as a potential audit in the ANAO’s 2014 Audit Work Program.<sup>93</sup>

## Committee comment

### Assessment and funding stages

- 2.59 A key conclusion of the ANAO audit, as noted by the Auditor-General, was that there was ‘not a clear trail through the various assessment stages adopted in [RDAF] rounds three and four to demonstrate that the projects recommended for funding, and those ultimately awarded funding, had

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87 The NSRF is a competitive regional grants program to fund priority infrastructure in regional communities, with \$1 billion in funding to be provided over five years from 2015-16 – see DIRD website on the NSRF, <http://investment.infrastructure.gov.au/funding/NSRF> (accessed May 2015).

88 See Mr Andrew Jagers, Executive Director, Infrastructure Investment Division, DIRD, *Committee Hansard*, Canberra, 6 March 2015, pp. 15-17, 23.

89 Mr Jagers, DIRD, *Committee Hansard*, Canberra, 6 March 2015, p. 15.

90 Ms O’Connell, DIRD, *Committee Hansard*, Canberra, 6 March 2015, p. 15.

91 Mr Jagers, DIRD, *Committee Hansard*, Canberra, 6 March 2015, p. 17.

92 Mr Boyd, ANAO, *Committee Hansard*, Canberra, 6 March 2015, p. 17.

93 Mr Boyd, ANAO, *Committee Hansard*, Canberra, 6 March 2015, p. 15 – see ANAO, *Audit Work Program*, July 2014, p. 90.

the greatest merit in terms of the published selection criteria'.<sup>94</sup> (Differing views expressed by the RDAF advisory panel and the then Minister on some aspects of the ANAO report are noted below.)

- 2.60 In terms of the department's role in assessing RDAF applications, the Committee was pleased to note the ANAO's finding that 'improvements in the quality of the department's assessment work' evident from the first RDAF round audited by ANAO 'continued in the third and fourth funding rounds'.<sup>95</sup> However, the Committee notes that the ANAO found there remained 'significant shortcomings' with the department's assessment methodology for rounds three and four, including that: the qualitative rating scale used by the department did not provide a 'clear and consistent basis for effectively discriminating between the relative merits of competing applications'; there was an 'unsound methodology for assessing value with public money'; and the department had not fully implemented recommendations from the previous ANAO report on the first RDAF round designed to address these shortcomings.<sup>96</sup> (Implementation of ANAO recommendations by the department and DIRD's comments on this matter are further discussed below.)
- 2.61 In terms of the advisory panel's role in assessing RDAF applications, the Auditor-General pointed to concerns with the panel not having documented an assessment of each application against each selection criterion to support or explain its recommendations.<sup>97</sup> While the ANAO has no fundamental issue with the advisory panel reaching a different view from the department as to the individual or relative merits of applications, as the Auditor-General noted, this approach meant that the 'demotion of some projects and promotion of others compared with the only recorded ratings awarded against the selection criteria (being the department's) was unexplained'.<sup>98</sup>
- 2.62 The Committee supports the ANAO's recommendations to address this matter from the current and previous RDAF audits. In particular, the Committee supports the ANAO recommendation that, in its administration of future grants programs and consistent with the key principles for grants administration outlined in the Commonwealth Grants Rules and Guidelines, DIRD – working with advisory panels, where relevant – improve the assessment of individual applications against each of the published program selection criteria to promote a clear

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94 Mr McPhee, ANAO, 'Opening statement', *Submission 2*, p. 2.

95 ANAO, Audit Report No. 9 (2014-15), p. 22.

96 ANAO, Audit Report No. 9 (2014-15), p. 22.

97 Mr McPhee, ANAO, 'Opening statement', *Submission 2*, p. 2.

98 Mr McPhee, ANAO, 'Opening statement', *Submission 2*, p. 2.



alignment between these assessments and the order of merit for funding recommendations. The Committee also believes there may be merit in the ANAO considering the inclusion of a specific reference, where relevant, in the objective, scope and criteria of future audits of regional grants administration to assessing how advisory panels have met their obligations under the Commonwealth Grants Rules and Guidelines, to further reinforce the significance of this matter.

- 2.63 The advisory panel's response to the ANAO report and the ANAO comment on this matter are noted.<sup>99</sup> The Committee believes there may be merit in the Department of Finance and the ANAO reviewing whether the Commonwealth Grants Rules and Guidelines and section 3.2.2, 'Use of an advisory panel in the selection of grant recipients', of the *Implementing Better Practice Grants Administration* guide could usefully be further revised to reinforce the ANAO's RDAF audit findings concerning the obligations of advisory panels in grant funding programs, particularly in terms of documentation and published program selection criteria.
- 2.64 In terms of the then Minister's funding decisions, the Committee notes the ANAO's finding that the approach taken by the department and the advisory panel to advising the then Minister as to which RDAF round three and four applications should be awarded funding had a number of 'significant shortcomings', including that applications were 'banded into a small number of categories', offering the then Minister 'limited assistance in terms of delineating the relative merits of competing applications', and that the briefing materials were 'voluminous', with insufficient summary material provided by the department, making it 'difficult for any decision-maker to compare the assessed merits of competing applications'.<sup>100</sup> This was exacerbated by numerous errors in the snapshot assessments and significant differences in assessment of projects between DIRD and the panel that covered at least a third of applications. Further, notwithstanding that the department had indicated it would review and enhance the documentation provided to the Minister to ensure the outcomes of the assessment aligned with the order of merit for funding recommendations, 'no improvement was evident in this regard'.<sup>101</sup> As the ANAO commented, 'there were a number of issues. Some of them would not have been visible, but the fact is that ministers, from our perspective,

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99 For the advisory panel's response to the ANAO report, together with the ANAO comment, see Appendix 3, 'Former RDAF Advisory Panel's response', Audit Report No. 9 (2014-15), pp. 167-181.

100 ANAO, Audit Report No. 9 (2014-15), p. 26.

101 ANAO, Audit Report No. 9 (2014-15), p. 131.

should be able to rely upon departments and panels getting that right for them'.<sup>102</sup>

- 2.65 The Committee supports the ANAO recommendation to improve the quality and clarity of future advice provided by the department to ministers on the merits of proposed grants under a merit based competitive selection process – in particular, that DIRD provide advice that clearly and consistently establishes the comparative merit of applications relative to the program guidelines and merit criteria, and includes a high level summary of the assessment results of each of the competing proposals in terms of their merit against the published criteria.
- 2.66 As well as significant disagreements regarding assessment rankings between the department and the advisory panel for RDAF rounds three and four, the ANAO pointed to a lack of alignment between assessment and funding stages – specifically, that the then Minister rejected 41 applications that had been recommended for funding by the advisory panel and approved 33 applications that had not been recommended – of which 10 had been categorised as 'Suitable for Funding' and 23 had been categorised as 'Not Recommended for Funding' by the panel.<sup>103</sup>
- 2.67 An issue that emerged here concerned a difference in opinion as to whether or not RDAF projects classified as 'Suitable for Funding' were available for selection by the Minister, and whether or not the Minister therefore had to report to the Finance Minister approval of any grant application from this category.<sup>104</sup> The response of the then Minister to the ANAO report as regards this matter and the ANAO comment are noted.<sup>105</sup> DIRD confirmed at the Committee hearing that the Minister followed the clear advice of the department regarding which project selections required notice being given to the Finance Minister. These projects were then reported to the Finance Minister.<sup>106</sup> The Committee agrees with the ANAO that the then Minister's response highlights that the 'Suitable for Funding' descriptor was 'not a particularly helpful descriptor' and that this points to the benefit of DIRD, in future granting activities, providing a clear statement for each grant proposal to either approve or reject the proposal.<sup>107</sup> This would in turn improve clarity in terms of determining the requirement to report to the

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102 Mr Boyd, ANAO, *Committee Hansard*, Canberra, 6 March 2015, p. 6.

103 Mr McPhee, ANAO, 'Opening statement', *Submission 2*, p. 3.

104 See *Committee Hansard*, Canberra, 6 March 2015, pp. 7-8, pp. 12-13; and ANAO, Audit Report No. 9 (2014-15), pp. 17-18.

105 See the response of the then Minister to the ANAO report and the ANAO comment at Appendix 2, Audit Report No. 9 (2014-15), pp. 164-166.

106 Ms O'Connell, DIRD, *Committee Hansard*, Canberra, 6 March 2015, p. 7.

107 ANAO, Audit Report No. 9 (2014-15), p. 29.

Finance Minister on such matters. The Committee believes there may be merit in the Department of Finance and the ANAO reviewing whether the Commonwealth Grants Rules and Guidelines and the *Implementing Better Practice Grants Administration* guide could usefully be further revised to reinforce this point.

- 2.68 However, the Committee notes that the ANAO pointed to a broader issue here regarding the requirement for decision-makers to record the basis for funding decisions. As the Auditor-General observed, while it is open to a Minister to reach a decision different from that recommended by an advisory panel or department, 'it is important that the rationale for such decisions be documented and be consistent with the published program guidelines and with any other applicable Commonwealth policies and legislation'. However, where the then Minister's funding decisions diverged from the recommendations of the advisory panel in RDAF rounds three and four, the 'recorded reasons did not refer explicitly to the published selection criteria and generally provided little insight'.<sup>108</sup> The Committee notes that the grants administration framework has been 'designed to accommodate situations where decision-makers do not accept the advice they receive' and, amongst other things, 'it requires that the basis for funding decisions be recorded'.<sup>109</sup>
- 2.69 The Committee makes recommendations concerning these matters below.

## Transparency and accountability

- 2.70 The ANAO found that, in a number of important respects, the conduct of the third and fourth RDAF funding rounds was 'not consistent with the accountability and transparency principles outlined in the grants administration framework'.<sup>110</sup> In terms of the funding decisions that diverged from the advisory panel's recommendations in rounds three and four, the Auditor-General noted that this 'situation was particularly significant given that such decisions were largely at the expense of projects located in electorates held by the Coalition'.<sup>111</sup>
- 2.71 Despite the shortcomings identified in the ANAO report, the Committee notes that the incoming Minister made a decision to continue and fund all projects in rounds three and four. This included both contracted and uncontracted projects.<sup>112</sup>

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108 Mr McPhee, ANAO, 'Opening statement', *Submission 2*, p. 3.

109 ANAO, Audit Report No. 9 (2014-15), p. 18.

110 ANAO, Audit Report No. 9 (2014-15), p. 29.

111 Mr McPhee, ANAO, 'Opening statement', *Submission 2*, p. 3.

112 Ms O'Connell, DIRD, *Committee Hansard*, Canberra, 6 March 2015, p. 5.

- 2.72 The ANAO explained that it was common practice for relevant ANAO reports to consider the electoral distribution of funding as a measure to evaluate program equity.<sup>113</sup> The Committee understands that the ANAO Better Practice Guide on *Implementing Better Practice Grants Administration* and the Commonwealth Grants Rules and Guidelines also make reference to this matter.<sup>114</sup>
- 2.73 The Committee supports the continuing emphasis on this area in relevant ANAO audits in order to continue to improve transparency and accountability in grants administration. The Committee also supports the emphasis that the Commonwealth Grants Rules and Guidelines have placed on this area, in specifically making reference to the ANAO's practice concerning this matter: '[T]he ANAO has emphasised that those involved in grants administration should ... be aware that the geographic and political distribution of grants may be seen as indicators of the general equity of a programme'.<sup>115</sup>
- 2.74 The Committee notes the issues raised at the public hearing concerning the ANAO's reference in its report to an AEC classification of electorates as 'rural or provincial'.<sup>116</sup> The Committee notes that some electorates classified as 'outer metropolitan' contain regional areas.<sup>117</sup> The Committee suggests that in the next update of the Better Practice Guide, *Implementing Better Practice Grants Administration* – specifically regarding section 8.8, 'Equity of distribution of program funds' – the ANAO (in consultation with the AEC as required) may wish to further clarify its potential use of such AEC classifications in its performance audit reports.
- 2.75 The Committee makes recommendations concerning these matters below.

## Implementation of ANAO report recommendations

- 2.76 The Committee notes the ANAO finding that the recommendations made in its previous audit of the design and conduct of RDAF round one, as agreed by the department, had 'not been implemented by the department'.<sup>118</sup> DIRD's differing view regarding the department's

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113 Mr McPhee, ANAO, *Committee Hansard*, Canberra, 6 March 2015, p. 19. See also ANAO, *Submission 2.1*, p. 2.

114 ANAO, *Implementing Better Practice Grants Administration*, Better Practice Guide, December 2013, p. 94 – quoted in ANAO, *Submission 2.1*, pp. 2-3; and *Commonwealth Grants Rules and Guidelines*, July 2014, paragraph 13.9, p. 35 – quoted in *Submission 2.1*, p. 3.

115 *Commonwealth Grants Rules and Guidelines*, July 2014, paragraph 13.9, p. 35 – quoted in ANAO, *Submission 2.1*, p. 3.

116 ANAO, Audit Report No. 9 (2014-15), pp. 150-151.

117 Mr Boyd, ANAO, *Committee Hansard*, Canberra, 6 March 2015, p. 19.

118 ANAO, Audit Report No. 9 (2014-15), p. 16.

progress in implementing these recommendations is noted.<sup>119</sup> However, the Committee agrees with the Auditor-General that closer adherence to implementing ANAO recommendations – which often reflect ANAO’s experience of practices other departments have found to be beneficial – warrants ‘greater attention by the department’.<sup>120</sup>

- 2.77 Accordingly, the Committee was pleased to note DIRD’s progress in implementing the recommendations from the ANAO report on RDAF rounds three and four, as outlined at the public hearing.<sup>121</sup>
- 2.78 The Committee supports the ANAO’s recommendations from the current and previous RDAF audits to improve the effectiveness of DIRD’s grants administration. Implementation of audit recommendations has been an ongoing focus of the ANAO and JCPAA.<sup>122</sup> The Committee believes it would be useful for the ANAO to consider prioritising DIRD (or, as applicable, the department responsible for administering the regional portfolio) in its continuing series of audits of agencies’ implementation of performance audit recommendations.

### Recommendation 1

- 2.79 **The Committee recommends that the Australian National Audit Office consider prioritising the Department of Infrastructure and Regional Development – or, as applicable, the department responsible for administering the regional portfolio – in its continuing series of audits of agencies’ implementation of performance audit recommendations.**

### Better practice regional grants administration

- 2.80 The ANAO has undertaken performance audits of ‘each of the major regional grant funding programs introduced by successive governments over the last eleven years’.<sup>123</sup> The Committee was pleased to hear that, over this period, ‘improvements have been observed in some important aspects

119 See DIRD, *Submission 1*, p. 1. DIRD provided further details on how it had implemented these recommendations – see Ms O’Connell, DIRD, *Committee Hansard*, Canberra, 6 March 2015, p. 2; and *Submission 1*, pp. 2-3.

120 Mr McPhee, ANAO, ‘Opening statement’, *Submission 2*, p. 4.

121 Ms O’Connell, DIRD, *Committee Hansard*, Canberra, 6 March 2015, p. 1.

122 See, for example, ANAO, Audit Report No. 53 (2012-13), *Agencies’ Implementation of Performance Audit Recommendations*; and JCPAA, ‘Chapter 2: Defence’s implementation of audit recommendations’ and ‘Chapter 3: Agencies’ implementation of audit recommendations’ in *Report 443: Review of Auditor-General’s Reports Nos. 23 and 25 (2012-13) and 32 (2012-13) to 9 (2013-14)*.

123 ANAO, Audit Report No. 9 (2014-15), pp. 19-20.

of the design and implementation of regional grant programs'.<sup>124</sup> However, the Committee notes the ANAO finding that, in this context, the 'most important message from this audit is that considerable work remains to be done to design and conduct regional grant programs in a way where funding is awarded, and can be seen to have been awarded, to those applications that demonstrate the greatest merit in terms of the published program guidelines'.<sup>125</sup>

2.81 Noting these continuing concerns in achieving better practice regional grants administration, the Committee believes that further improvement in this area might best be achieved through a range of approaches, including:

- Priority follow-up audits of the effectiveness of DIRD's grants administration, with a standing audit focus on regional grants administration
- Revision of the Commonwealth Grants Rules and Guidelines and ANAO Better Practice Guide, *Implementing Better Practice Grants Administration*, by the Department of Finance and the ANAO, as required, to reflect findings and recommendations of ANAO performance audit reports and JCPAA reports relevant to this area
- Priority ANAO follow-up of DIRD's implementation of audit recommendations
- Addition of a new section on 'Regional grants administration' in the ANAO Better Practice Guide, *Implementing Better Practice Grants Administration*
- An increased focus on training of departmental officers in this area, as required, by the Department of Finance

2.82 The Committee commends the Department of Finance and the ANAO on the development of the Commonwealth Grants Rules and Guidelines and the Better Practice Guide, *Implementing Better Practice Grants Administration*. The ANAO's Better Practice Guide is an important document in bringing together collective experience on this matter. As DIRD remarked at the public hearing, the guide is a 'particularly seminal and useful document to point out the way that the ANAO thinks that grants are best administered'.<sup>126</sup>

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124 ANAO, Audit Report No. 9 (2014-15), p. 20.

125 ANAO, Audit Report No. 9 (2014-15), p. 21.

126 Ms O'Connell, DIRD, *Committee Hansard*, Canberra, 6 March 2015, p. 10.

## Recommendation 2

- 2.83 The Committee recommends that in the next update of its Better Practice Guide, *Implementing Better Practice Grants Administration*, the Australian National Audit Office (ANAO) consider incorporating a new section on 'Regional grants administration', focusing on the findings of recent ANAO reports on this area and the Committee's report, to maintain an emphasis on increased effectiveness in regional grants administration.

## Recommendation 3

- 2.84 The Committee recommends that the Department of Finance, in consultation with the Australian National Audit Office (ANAO), update, as required, the Commonwealth Grants Rules and Guidelines to reflect recent ANAO audit findings concerning departmental grants administration, including further reinforcing the requirement for decision-makers to record the basis for funding decisions.
- 2.85 The Committee commends the ANAO for its continuing focus on auditing regional grants programs and notes the Auditor-General's salient point about the 'long-term gain' from such audit processes and the responses by the department over time.<sup>127</sup>
- 2.86 The Committee was pleased to note DIRD's assurance that in designing the new National Stronger Regions Fund (NSRF) the department has 'taken into account the ANAO's recommendations and adjusted the way that program will operate accordingly'.<sup>128</sup> The Committee is aware that the design and implementation of the NSRF, including the processes by which projects are awarded funding, is listed as a potential audit in the ANAO's 2014 Audit Work Program.<sup>129</sup>
- 2.87 The Committee notes the Auditor-General's conclusion that closer adherence to relevant aspects of the grants administration framework is a matter that warrants 'greater attention by the department',<sup>130</sup> and that 'considerable work remains to be done to design and conduct regional grant programs in a way where funding is awarded, and can be seen to

127 Mr McPhee, ANAO, *Committee Hansard*, Canberra, 6 March 2015, p. 23.

128 Mr Jaggars, DIRD, *Committee Hansard*, Canberra, 6 March 2015, p. 15.

129 ANAO, *Audit Work Program*, July 2014, p. 90.

130 Mr McPhee, ANAO, 'Opening statement', *Submission 2*, p. 4.

have been awarded, to those applications that demonstrate the greatest merit in terms of the published program guidelines'.<sup>131</sup>

- 2.88 Accordingly, the Committee believes there would be merit in the ANAO conducting priority follow-up audits of the effectiveness of DIRD's grants administration, and also adopting a standing priority audit focus on the design and conduct of future regional grants programs, to ensure a continued emphasis on effectiveness in this area. These audits could also usefully consider the effectiveness of the department's ongoing implementation of relevant ANAO recommendations.

#### **Recommendation 4**

- 2.89 **To encourage better practice grants administration, particularly concerning regional grants programs, the Committee recommends that the Australian National Audit Office (ANAO) consider including in its schedule of performance audits:**
- **priority follow-up audits of the effectiveness of grants program administration by the Department of Infrastructure and Regional Development**
  - **a standing priority audit focus on regional grants administration by the relevant department (with the specific timing of such audits as determined by the ANAO), noting that a potential performance audit of the design and implementation of the National Stronger Regions Fund is included in the ANAO's current forward Audit Work Program**

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131 ANAO, Audit Report No. 9 (2014-15), p. 21.