8 September 2008

Mr Russell Chafer
Committee Secretary
Joint Committee of Public Accounts and Audit
PO Box 6021
Australian Parliament House ACT 2600

Re: Inquiry into the impact of the efficiency dividend on small agencies

Dear Mr Chafer,

I am writing in response to questions taken on notice when representatives of the Academy, Professors Graeme Clarke and Deryck Schreuder, appeared before the Committee on 21 August 2008. I regret that I was unable to attend the hearing on account of being out of the country, and was therefore unable to tender detailed advice to supplement the excellent testimony of Professors Clarke and Schreuder.

On page PA47 of the proof Committee Hansard, the Chair noted that the Academy would not support a 'sliding scale' measure. This question goes to our response to question 6 of the inquiry terms of reference, which concludes by asking 'whether the rate of the dividend should vary according to agency size or function.' We answered that we do not favour such a response, because it promised not to halt the decline but merely drew it out. Our problem with the efficiency dividend is fundamental, and so changing the size of it, or applying it in different measure to different agencies on whatever basis, does nothing to change that.

We have additional technical reservations: we have seen no evidence of any correlation between agency size and the effect of the dividend in percentage terms, so applying relief on this basis would seem spurious. Also, differential relief made on the basis of agency function will be even more invidious, as it will imply value judgments about the virtue of the agencies. But our fundamental objection renders these issues irrelevant.

Our core point is that the efficiency dividend is the wrong instrument to employ if the objective is to keep mission-directed agencies delivering services as their charters require. These organisations have been charged with a task by government, with the consent and support of the public at large, but they are increasingly hampered in their ability to deliver on their responsibilities due to the tightening strictures of the efficiency dividend. Their service charters, organisational structures and missions make them entirely unlike the departments, yet they are subject to a measure that was designed for application to the departments (and with which the departments are able to find ways to live) Our earnest recommendation is that the efficiency dividend should be replaced in the instance of the mission-directed agencies, such as the cultural institutions, and replaced by other methods of ensuring value for money and effective service delivery.

Also on page PA47, our reference to an ERC advisory group was mentioned. This was presented as a back-up idea to help introduce a method to deal sensibly with the effects of the efficiency dividend in the event that it is left in place. In those circumstances, it would be our advice that a modest sum be made available for distribution between the relevant institutions on the basis of demonstrated need. Given the cross-portfolio nature of the problem, it seems likely that the decisions would be most appropriately made by the ERC on the advice of an expert advisory group. We are well aware of the likely difficulty in arriving at sound, comparative evidence-based decisions: in the absence of the suspension of the efficiency dividend, however, this does seem to be the most appropriate means by which to deal with a significant and growing problem for government.

On page PA48, the Chair made mention of our suggestion of the establishment of an Australian cultural investment fund. This idea is underpinned by the notion that our cultural educational resources are every bit as important as the formal educational institutions to be supported by the Education Investment Fund. The proposal seeks to emulate the EIF structure, relying on the expertise within the Future Fund to generate revenues which could be invested in our valuable – and popular – cultural institutions. It is our view that there would be a lot of public support for a move to earmark a modest portion of the forecast budget surplus to help our libraries, museums, archives and galleries stay open longer, provide a broader range of services, with up-to-date technology and top-level reciprocal access to overseas collections.

Having recommended the abolition of the efficiency dividend for these small agencies, we would also like to respond to the most reasonable concerns raised by the Chair on page PA54 of the proof Committee Hansard. She asks, ‘If there was a recommendation that cultural organisations or these sorts of national academic institutions be exempt from an efficiency dividend, what would the process be for quality assurance regarding value for money, accountability and efficiency gains?’ Senator Hogg backed this up shortly after by asking ‘how government assures itself that not only is there leanness and meanness in the organisation—and that might not necessarily be the criteria—but also it is an efficient organisation?’

As Professor Schreuder indicates, the Academy has no difficulty with the value argument, and agrees that we cannot simply live with the virtue argument anymore. Professor Schreuder then cited the usage data as tangible and compelling extrinsic evidence for our case, as they show that the institutions are as well patronised as they can be within the constraints applied by the dividend, and that they are poised to deliver still better value for money if they were only funded appropriately.

Elsewhere, though, the need to convince the hard-nosed officials whose job it is to scrutinise budgets was mentioned, so we have a point or two to add to that end in closing. We have mentioned that the efficiency dividend is not the right tool for the job. There are several reasons for this, due to questions of: scale; desired standards; minimum standards and fitness for purpose.

Scale. The theory of the efficiency dividend breaks down in practice when applied to organisations below a threshold size. The measure was devised for large departments many times larger than the unit of service delivery: in smaller agencies, another 2% can literally mean the cessation of an entire stream of activity.

Desired standards. Efficiency is not a variable in its own right, but a ratio, of effectiveness relative to resources. This ratio works fine over a wide band of effectiveness, and it finds its expression in the market place in the diversity of good available of various qualities on a price spectrum. This is what people mean by 'value for money': it is a form of efficiency, expressed in financial terms.. But before we grab the cheapest gadget and just head for the check-out, we usually like to make a conscious decision about the level of quality we expect. In the case of mission-directed small agencies, they might argue that this desired quality standard is implied in their charters. What every consumer then knows is that we then need to be prepared to pay for that desired level of quality. The efficiency dividend erodes our ability to choose our desired level of quality by applying a reduction algorithmically, without us ever making the conscious choice that we wish to go low-end – which is, of course, where we can only end up.

Minimum standards. This line of thought leads to the idea of a minimum standard of quality. In any ratio of bang for buck, there is a lower level of effectiveness (or value) below which it doesn't matter how cheaply you have procured your gadget: it simply doesn't work well enough for the purchase to have been worthwhile. You put it in the cupboard and never get it out again, and you've simply done your dough on nothing. This is the conceptual limits of the notion of efficiency. It is not value for money, because the 'value' is effectively zero below a certain level. So applying an efficiency paradigm without heed to how unstable the ratio becomes in practice at small values is self-defeating.

Fitness for purpose. The efficiency dividend is designed to be applied to departments with broad briefs and constant policy renewal, features which they exploit to bring new revenue streams in from the side to compensate for the efficiency dividend. These features are not generally shared by the small agencies, as discussed at length in our submission and those of many others.

We realise this leaves unaddressed some of the Committee's legitimate concerns about mechanisms for oversight on questions of quality and efficiency. It is our view that a dumb formula like the efficiency dividend is no substitute for actual scrutiny, and we would be very surprised if the existing means of reporting and performance measurement were not already quite capable of satisfying Parliament on those questions in the case of the cultural institutions. If current reporting standards need further work to provide the desired level of accountability, or to be sufficiently comparable to one another, we are confident that this could be done without an inordinate amount of work.

If all else fails, we would speculate that there must presumably be some people working on the kinds of guarantees of quality, efficiency and value for money that will need to take the place of the efficiency dividend in the case of the Australian Defence Force (which is exempt, and whose budget, we venture, is many times the total of all the small agencies in question). Perhaps the answers to some of those questions regarding the ADF could assist with some of these important oversight issues with regard to small agencies, including the cultural institutions.

As always, please do not hesitate to contact me should there be anything upon which I can provide further information or assistance. I congratulate the Committee on its excellent work and wish it well in its deliberations.

Kind regards,

Dr John Byron
Executive Director