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The Parliament of the Commonwealth of Australia

# **Report 398**

**Review of Auditor-General's Reports 2002-2003  
Fourth Quarter**

**Joint Committee of Public Accounts and Audit**

March 2004  
Canberra

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## Foreword

The outcomes of the review by the Joint Committee of Public Accounts and Audit of the Auditor-General's audit reports tabled in the fourth quarter of 2002–2003 are presented in the Committee's **Report 398**. Of the 34 audit reports reviewed, the Committee selected three for further examination at public hearings, respectively Audit Report No. 42, 2002–2003, *Managing Residential Aged Care Accreditation*; Audit Report No. 51, 2002–2003, *Defence Housing and Relocation Services*; and Audit Report No. 55, 2002–2003, *Goods and Services Tax Fraud Prevention and Control*.

The Committee's interest in reviewing Audit Report No. 42, 2002–2003, *Managing Residential Aged Care Accreditation*, was triggered by observations by the Australian National Audit Office that the relatively recently introduced aged care accreditation process still showed significant levels of operational and financial volatility. Further, in reviewing this report, the Committee recognises the importance of a rigorous and efficient accreditation system in the future delivery of quality aged care to an ageing Australian population.

Although accreditation of residential aged care facilities was established in 1997, the Aged Care Standards and Accreditation Agency Ltd could not commence audits until the gazettal of principles in September 1999. This left the Agency with a severe time constraint which contributed to inefficiencies, and to inconsistencies in judgements and decisions during the first round of accreditations.

The Committee notes, however, that many of the early problems associated with maintaining accreditation standards deriving from the peaking of the Agency's workload around three-year accreditation cycles, are now being resolved. Whereas full-time staff could not cope with the workload when most first round accreditations were undertaken, the hiring and training of temporary employees and the distribution of guidance manuals to all assessors for second round work has alleviated many of the earlier problems. The Committee is satisfied that an acceptable level of consistency was achieved during the second cycle of accreditation which is now complete.

The Committee has concerns, however, that despite all the efforts put into setting up and running the accreditation process, witnesses at the public hearing were unable to give clear indications that the quality-of-life of residents of aged care facilities has actually improved. Monitoring the effectiveness of accreditation in delivering better quality aged care services appears to rest solely on clinical quality data rather than some combination that includes a broader set of quality-of-life measures. Accordingly, the Committee recommends that the Aged Care Standards and Accreditation Agency develop a better quality monitoring mechanism that includes a balance of objective clinical quality data and subjective quality-of-life measures. In making this recommendation, the Committee is adamant that the new mechanism must not impose additional compliance costs on the aged care facilities nor further complicate the accreditation system.

The Committee's review of Audit Report No. 51, 2002–2003, *Defence Housing and Relocation Services* addresses the efficiency and effectiveness of the agreement between the Department of Defence and the Defence Housing Authority in managing the provision of housing services to Australian Defence Force personnel. The Defence Housing Authority operates as an independent commercial entity providing services to the Department of Defence according to the provisions of the existing 10-year \$3.5 billion Service Agreement.

The Committee examined aspects of the Service Agreement, the relevance of the legal advice available during the writing of the Service Agreement, and the conflicting objectives of the two agencies. It finds that legal advice provided to the Department of Defence was not explicit enough for its Service Agreement obligations. Further, the Australian Defence Force's housing demand is unlikely to be met cost-effectively by market supply due to inflexibility in the housing classifications.

The Committee concludes that the requirement for the board of the Defence Housing Authority to include Australian Defence Force personnel connotes a potential conflict of interest and recommends that the *Defence Housing Authority Act 1987* be amended to remove the requirement to have three Australian Defence Force personnel on its board. There needs to be a complementary mechanism to ensure that Australian Defence Force personnel have a voice in strategic decisions affecting their housing. The Committee recommends therefore that the role of the existing Defence Domiciliary Group be expanded to include a formal consultation function with the Defence Housing Authority.

The Committee finds that the vacant housing issue has been tackled effectively by the Defence Housing Authority, cost-reductions have been achieved, and the quality maintenance fee is an effective mechanism to provide a superior service tailored to Australian Defence Force personnel needs.

A range of outstanding issues identified by the Australian National Audit Office including the establishment of continuous improvement programs, Key Performance Indicators, a property register and a review of deemed effective markets was not convincingly explained by the Department of Defence. The



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Committee recommends that the Department of Defence report to the Australian National Audit Office and to the Committee on its progress in rectifying these matters.

Audit Report No. 55, 2002–2003, *Goods and Services Tax Fraud Prevention and Control* addresses a major tax revenue loss area. The Australian National Audit Office identified, and the Australian Taxation Office agreed, that controlling Goods and Service Tax fraud poses a significant challenge for the Australian Taxation Office.

The Committee is pleased to note that Australia's Goods and Services Tax system compares favourably with systems of similar type used overseas, in the main due to thorough preparatory research by the Australian Taxation Office of relevant international value added tax regimes.

The Committee is concerned with the prevalence and potentially destructive impact of cash economy Goods and Services Tax avoidance. Determining the magnitude of the cash economy has proved to be difficult. The Committee endorses, however, the efforts that the Australian Taxation Office has taken to capture tax owing on cash transactions using a variety of tools. Australian Business Number registration and monitoring has been particularly successful.

Australian Taxation Office has up-graded its non-compliance capability since the Australian National Audit Office audit, by merging three non-compliance functions. Similarly, the Australian Taxation Office is in the process of installing a new case management system that will record and report on Goods and Services Tax fraud. The Committee notes that testing the efficacy of the new system has still to be finalised and recommends that the Australian Taxation Office provide a report on its effectiveness to the Australian National Audit Office and to the Committee when installation is complete.

To date *major* fraud has been targeted for investigation and prosecution. The Committee is pleased that *minor* fraud is increasingly being captured cost-effectively using tools such as a tax evasion hot line.

The Committee feels that a rigorously derived estimate of the tax gap is required as an input to successful monitoring of prevention and control of Goods and Services Tax fraud.

The Australian Taxation Office's Risk Rating Engine and its tandem Registration Information Matching System appear to be assessing tax payer risk and registration compliance effectively.

The Committee is concerned that instances of "borderline fraud" are escaping prosecution. It concurs that a logical response to controlling this category of fraud is to tighten the appropriate statutes so that the ease of proof of fraud is enhanced, and it makes a recommendation accordingly.

In conclusion the Committee commends the three agencies that were the subject of these reviews, for their overall early and positive responses to the respective Australian National Audit Office audit outcomes.

**Mr Bob Charles MP**  
**Chairman**



## **Membership of the Committee**

**Chairman** Mr Bob Charles MP

**Deputy Chair** Ms Tanya Plibersek MP

**Members**

Senator John Hogg	Mr Steven Ciobo MP
Senator Gary Humphries	Mr John Cobb MP
Senator Kate Lundy	Mr Petro Georgiou MP
Senator Andrew Murray	Mr Alan Griffin MP
Senator Nigel Scullion	Ms Sharon Grierson MP
Senator John Watson	Ms Catherine King MP
	Mr Peter King MP
	The Hon Alex Somlyay MP

## **Membership of the Sectional Committee**

**Chairman**     Mr Bob Charles MP

**Deputy Chair**   Ms Tanya Plibersek MP

**Members**     Senator John Watson

Ms Catherine King MP

Ms Sharon Grierson MP

The Hon Alex Somlyay MP

## **Committee Secretariat**

**Secretary**             Mr James Catchpole

**Inquiry Secretary**     Mr Frederick Cook

**Research Officer**     Mr Alex Stock



## List of abbreviations

ABN	Australian Business Number
ABS	Australian Bureau of Statistics
AC Act	<i>Aged Care Act 1997</i>
ACSA	Aged and Community Services Australia
ADF	Australian Defence Force
AFP	Australian Federal Police
AGD	Attorney-General's Department
the Agency	Aged Care Standards and Accreditation Agency Ltd
ANAO	Australian National Audit Office
ANHECA	Australian Nursing Homes and Extended Care Association
ATO	Australian Taxation Office
CAC Act	<i>Commonwealth Authorities and Companies Act 1997</i>
CHA	Catholic Health Australia
DDG	Defence Domiciliary Group
Defence	Department of Defence
DHA	Defence Housing Authority
DHA Act	<i>Defence Housing Authority Act 1987</i>
DOC	Domiciliary Operations Committee
DPP	Commonwealth Director of Public Prosecutions

FIRM	Fraud Investigation Reporting and Management system
FMA Act	<i>Financial Management and Accountability Act 1997</i>
GBE	Government Business Enterprise
GST	Goods and Services Tax
Health	Department of Health and Ageing
JAS-ANZ	Joint Accreditation System of Australia & New Zealand
KPI	Key Performance Indicator
OECD	Organisation of Economic and Cultural Development
RIMS	Registration Information Matching System
RRE	Risk Rating Engine
VAT	Value Added Tax



# List of recommendations

## 2 Managing Residential Aged Care Accreditation

### Recommendation 1

The Aged Care Standards and Accreditation Agency Limited broaden the focus of the quality assessment data currently used for accreditation purposes, to include quality-of-life information experienced industry-wide by residents of aged care homes. Overall, the resultant data collection mechanism must not impose additional costs on the aged care facilities nor further complicate the accreditation system.

## 3 Defence Housing and Relocation Services

### Recommendation 2

Section 12 (1) of the *Defence Housing Authority Act 1987* be amended to remove the provision that the Defence Housing Authority include three members of the Australian Defence Force.

The *Services Agreement for Housing and Related Requirements* be amended to allow for a formal consultative process, possibly including the Defence Domiciliary Group, to enable the Department of Defence to advise Defence Housing Authority of Australian Defence Force housing requirements.

**Recommendation 3**

The Department of Defence report within six months to the Joint Committee of Public Accounts and Audit on its progress towards addressing the outstanding issues listed in Paragraph 4.6 of the Australian National Audit Office Audit Report No. 51, 2002–03, *Defence Housing and Relocation Services*.

**4 Goods and Services Tax Fraud Prevention and Control**

**Recommendation 4**

The Attorney-General's Department, in liaison with the Australian Taxation Office and the Commonwealth Director of Public Prosecutions, draft amendments to legislation, for the Attorney-General's consideration, that enhance the ease of proof in the prosecution of suspected Goods and Services Tax fraud.

**Recommendation 5**

The Australian Taxation Office report to the Joint Committee of Public Accounts and Audit within six months, on a mechanism to estimate the tax gap, that would serve as the basis for reporting the overall efficacy of the range of measures being adopted to prevent and control Goods and Services Tax fraud.



## Introduction

### Background to the review

- 1.1 The Joint Committee on Public Accounts and Audit has a statutory duty to examine all reports of the Auditor-General presented to the Presiding Officers of the Australian Parliament, and report the results of its deliberations to both Houses of Parliament. In selecting audit reports for review, the Committee considers:
- The significance of the program or issues raised in the audit reports;
  - The significance of the audit findings;
  - The arguments advanced by the audited agencies; and
  - The public interest of the report.
- 1.2 Upon consideration of 34 audit reports presented to the Parliament by the Auditor-General during the fourth quarter of 2002-2003, the Committee selected three reports for further scrutiny at public hearings. The public hearings were held in Canberra on:
- Monday 18 August 2003 (ANAO Audit Report No. 42);
  - Monday 15 September 2003 (ANAO Audit Report No. 51);
  - Monday 13 October 2003 (ANAO Audit Report No. 55).

## The Committee's Report

- 1.3 This report of the Committee's examination draws attention to the main issues raised at the respective public hearings. Where appropriate, the Committee has commented on unresolved or contentious issues and made recommendations.
- 1.4 The report is structured as follows:
- Chapter 2 - ANAO Audit Report No. 42 of 2002-2003 *Managing residential aged care accreditation* (Monday 18 August 2003);
  - Chapter 3 - ANAO Audit Report No. 51 of 2002-2003 *Defence housing relocation services* (Monday 15 September 2003);
  - Chapter 4 - ANAO Audit Report No. 55 of 2002-2003, *Goods and services tax fraud prevention and control* (Monday 13 October 2003);
  - Appendix A - conduct of the Committee's review;
  - Appendix B - list of submissions authorised;
  - Appendix C - list of exhibits received; and
  - Appendix D - list of witnesses who appeared at the public hearings.
- 1.5 A copy of this report is available on the Committee's website at <http://www.aph.gov.au/house/committee/jcpaa/reports.htm>.

## Audit Report No. 42, 2002–03

# Managing Residential Aged Care Accreditation

## Introduction

### Background

- 2.1 The aim of the Commonwealth's aged care program is to provide "support for healthy ageing for older Australians and quality and cost-effective care for frail older people and support for their carers"<sup>1</sup>. The principal methods of delivering aged care are community care and residential care.
- 2.2 The *Aged Care Act 1997* (AC Act) provides the framework for Commonwealth aged care funding and the administration of Commonwealth-funded aged care, and for the obligations of approved providers of aged care services.
- 2.3 Residential aged care homes are operated by the not-for-profit and private sectors, and by local and state governments. A new accreditation-based

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<sup>1</sup> Department of Health and Ageing (Health), *Portfolio Budget Statements 2002–03, Health and Ageing Portfolio, Budget Paper No. 1.11*, p. 99.

quality assurance system for residential aged care homes was proposed in the 1996–97 Budget. The Aged Care Standards and Accreditation Agency Ltd (the Agency) is the independent, wholly owned Commonwealth company that manages the accreditation process.

- 2.4 The Agency works with the Department of Health and Ageing (Health) to promote quality residential aged care. Health is responsible for ensuring homes meet their other obligations under the AC Act and for taking compliance action such as sanctions.

## The Audit

- 2.5 The Australian National Audit Office (ANAO) audit was conducted during July to September 2002. The objective was to determine whether the Agency's management of the residential aged care accreditation process was efficient and effective. It did not examine issues concerning the quality of care in residential aged care homes. However, it did examine whether the Agency was able to fulfil its statutory responsibilities.
- 2.6 Two rounds of accreditation had occurred since commencement of the accreditation process, pursuant to provisions of the AC Act, allowing the Agency scope to review a sample of its decisions. The audit focused on management of the accreditation process, by examining the Agency procedures that lead to accreditation decisions. The audit also included aspects of Health's role in the accreditation process.

## Audit Findings

- 2.7 While operating under challenging circumstances, the Agency had successfully assessed all residential aged care homes by 1 January 2001, as required by the AC Act, and had implemented a process to accredit and support services.
- 2.8 ANAO concluded that the Agency had adequately identified its legislative responsibilities for accreditation and had implemented an adequate process to meet them. In general, its management of its people and the workflow facilitated the accreditation process.
- 2.9 ANAO also concluded, however, that there were some weaknesses in the Agency's management systems which impact adversely on its implementation of the accreditation process. These included shortcomings in the Agency's costing systems, information management, and quality assurance mechanisms.

- 2.10 ANAO made six recommendations, all of which were agreed to by the Agency. In summary, the Agency should have a robust function for determining and allocating the costs of its functions; review its accreditation management information system; implement an analysis of the accreditation system; introduce performance indicators; plan an evaluation of the accreditation system on the quality of aged care; and review its quality mechanisms.
- 2.11 ANAO endorsed the Agency's positive responses to the audit and noted that the Agency was putting in place systems to correct the weaknesses raised during the ANAO audit.<sup>2</sup>

### The Committee's Review

- 2.12 On 18 August 2003 the Committee held a public hearing to review the progress made against ANAO's recommendations.
- 2.13 The public hearing was attended by the following organisations:
- Australian National Audit Office;
  - Department of Health and Ageing;
  - Aged Care Standards and Accreditation Agency Ltd;
  - Australian Nursing Homes and Extended Care Association;
  - Aged and Community Services Australia; and
  - Catholic Health Australia.
- 2.14 The Committee took substantive evidence on the following issues:
- Difficulties completing the accreditation process;
  - Assessor inconsistencies;
  - Measuring the effectiveness of accreditation and quality of aged care;
  - Costing methodology;
  - Training of nurses; and
  - Facility ownership.

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2 Australian National Audit Office (ANAO), *Transcript, 18 August 2003*, p. 13.

## Difficulties completing the accreditation process

- 2.15 The Committee noted the highly variable nature and intensity of the accreditation workload, essentially deriving from the three-year accreditation cycle. As all first round accreditations took place concurrently, reaccreditations similarly took place concurrently, but three years later. This tight cyclical pattern placed pressure on Aged Care Standards and Accreditation Agency Ltd (the Agency) to complete the bulk of its accreditation tasks, for each round, in a very short space of time. It coped by augmenting its team of full-time assessors by hiring contract assessors. Aged and Community Services Australia (ACSA), however, opined that this uneven workload was not an ideal arrangement in terms of ensuring consistency.<sup>3</sup>
- 2.16 Several witnesses including Catholic Health Australia (CHA), and Health concurred with, and elaborated on, this view.
- 2.17 ACSA observed that the uneven workload experienced by the Agency meant that the Agency had to take on extra staff to cope during the peak periods, making overall accreditation consistency a challenge. ACSA said that it favoured a broader accreditation arrangement whereby the Agency could be responsible for accrediting other aspects of clients' facilities in addition to aged care. In this way, ACSA reasoned, the Agency could spread its workload to ensure a more regular workflow and avoid a peak in one year and then a trough for the next two years, a situation which occurred when it only had to contend with aged care accrediting.<sup>4</sup>
- 2.18 CHA commented on the evolution of the accreditation system since its formation in October 1997. It noted that only after gazettal of the principles in September 1999 could the Agency commence audits. This imposed a time pressure situation, "not of its own making"<sup>5</sup>, on the Agency, particularly in terms of the first round of accreditation.
- 2.19 Health noted, however, that accreditation audits are just one part of the Agency's work cycle.

...continuous improvement models... is a job of work the Agency is doing continually.<sup>6</sup>

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3 Aged and Community Services Australia (ACSA), *Transcript, 18 August 2003*, p. 2.

4 ACSA, *Transcript, 18 August 2003*, p. 2.

5 Catholic Health Australia (CHA), *Transcript, 18 August 2003*, pp. 2-3.

6 Health, *Transcript, 18 August, 2003*, p. 3.

- 2.20 The Agency commented on the uneven work cycle deriving from the maximum period of grant of accreditation being three years, but it believed the matter to be more of a logistical issue than anything else. “To try to smooth it out artificially would be to destroy the integrity of the whole process, I suspect”.<sup>7</sup>
- 2.21 Clearly there is an uneven cycle to the actual accreditation work because almost all homes qualify concurrently for the maximum period of three years. A commencing service is entitled to a one year accreditation period only, but because of the comparatively small number involved, there is little scope for significant accreditation workload smoothing over time.
- ...the accreditation visit is just one part of the whole cycle of monitoring of homes. In the other years the agency... has a very big job to do outside the accreditation visits. I think it is an issue about workload. While the income might be slightly [peaky] the workload is pretty well distributed, albeit with a necessary decision-making load in one year—but I think the workload for visits is high across the whole time.<sup>8</sup>
- 2.22 The Agency pointed out there were benefits arising from the cyclical nature of the accreditation assessments activity including that some assessors with aged care experience were added to the assessment teams and in so doing, teams achieved an efficient mix of skills.<sup>9</sup>
- 2.23 The Agency advised the Committee that the task of training assessors was well advanced.

### Committee comment

- 2.24 The Committee notes that there is a peaking of the accreditation work load clearly due to the three-year cycle. However it feels that, on balance, any staggering of the accreditation process would not reduce the peaking significantly in early years. Artificial staggering would probably pose problems of its own (such as, how to choose the aged care homes that would be placed on a shorter term of accreditation, initially). Further, any natural smoothing by new entrants to the business would be insignificant given the very small number of new entrants as opposed to the thousands of existing homes.

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7 Aged Care Standards and Accreditation Agency Ltd (the Agency), *Transcript, 18 August 2003*, p. 3.

8 Health, *Transcript, 18 August 2003*, p. 11.

9 The Agency, *Transcript, 18 August 2003*, p. 3.

- 2.25 In the Committee's view, the Agency is coping with its uneven workload as well as could be expected, aided by scheduling its ongoing work in off-peak periods.

## Assessor inconsistencies

- 2.26 The Committee expressed concern that significant variations in compliance ratings recorded by assessors on a state-by-state basis as reported by ANAO<sup>10</sup>, may have resulted from different regulatory regimes set by different states, or involved varying judgements by different assessors, or indeed, variable performances by individual homes. Lack of consistency in accreditation standards clearly could result in, at best misleading, or at worst unjust accreditation outcome ratings.
- 2.27 ACSA opined that there was variability between assessors - different judgements by different people - during the first round but that that variability had been ironed out by the second round. The view put forward by the witness was that there was no robust mechanism, during the first round of accreditations, for establishing rating reliability between different teams.
- ...in the first round of accreditation the consistency of assessments was a major issue for the industry. We all had access to the statistics, and peers talking to peers could not believe there was a real difference in the quality of services of this order of magnitude, so we think it did come down to variability between individual assessors;...different judgments being applied by different people, and in that round of accreditation... there was no robust mechanism for establishing inter-rater reliability between the different teams...in place at the first round.<sup>11</sup>
- 2.28 CHA described how it has observed a "sea change" in the way the Agency performed its assessments, after the media reports of the kerosene bath affair in 2000 in the Riverside Nursing Home in Melbourne, leading the witness to question the fairness of assessments prior to the affair, compared to those undertaken after its exposure. CHA said that there appeared to be a significant point of change between the way facilities visited pre February 2000 and facilities visited post February 2000 were

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10 ANAO, Audit Report No. 42, 2002-2003, *Managing Residential Aged Care Accreditation*, p. 74.

11 ACSA, *Transcript, 18 August 2003*, pp. 3-4.



assessed, particularly in Victoria; there was an issue of lack of consistency.<sup>12</sup>

- 2.29 The administration and management of medication was put forward as a typical example of where variation could be expected, resulting in possible inconsistencies in accreditation. Different management styles could be expected from different nurses trained in different schools expressing differences in their professional judgments as to what is an adequate level of medication documentation.

They may have been trained differently. One or both of them has the power to write the report, but they could quite easily make a different judgment about what is a safe practice regarding medication.<sup>13</sup>

- 2.30 The Agency advised that the ratings categories had been simplified for the second round of accreditations to two categories - compliant and non-compliant.<sup>14</sup> As well much had been done to improve the skills of assessors including upgrading the level of training of the assessors, and introducing an assessor handbook and a results and processes handbook.

- 2.31 The Agency further advised that audit methodology training, involving a standardised assessment of all quality assessors doing round two assessments, was now compulsory for all assessors. Data are collected to determine the extent of any variations between assessors, in the ways they carry out audits. Further, efforts are being put in to determine the need for, and the development of, further training for assessors.<sup>15</sup>

- 2.32 Based on anecdotal feedback, the Agency advised that clients' opinions regarding its services had been favourable, and the Agency was complimented on the professionalism of its assessors, which "in this round has far exceeded the first round".<sup>16</sup>

### Committee comment

- 2.33 The Committee recognises that there is significant potential for inconsistencies in accreditation. It concludes that the problems noted

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12 CHA, *Transcript, 18 August 2003*, p. 4; The Agency, 2000, *Riverside Nursing Home Review Audit Reports*, 16 and 17 February, 25 pp; 29 February and 1 March 2000, 23 pp; Minister for Aged Care, 2000, *Delegates decision on elderly residents of Riverside Nursing Home*, Media Release 6 March 2000. Following the two review audits which rated the nursing home a "serious risk" against several criteria, the home was closed.

13 ACSA, *Transcript, 18 August 2003*, p. 4.

14 The Agency, *Transcript, 18 August 2003*, p. 5.

15 The Agency, *Transcript, 18 August 2003*, p. 10.

16 CHA, *Transcript, 18 August 2003*, p. 13.

during the first round have diminished in subsequent rounds in magnitude and importance, following the adoption by the Agency of a simplified ratings system. This system has reduced the likelihood of arbitrary assessor inconsistencies. As well, the Committee is satisfied that the Agency has improved the training of assessors and has upgraded the written guidelines for assessment.

- 2.34 The Committee also encourages the expansion of the practice of voluntary benchmarking by the industry, as a means of adding rigour to the accreditation process.

## **Measuring the effectiveness of accreditation and quality of aged care**

- 2.35 Witnesses were asked if data were available that could be analysed for incidence of quality failures in the services that aged care homes provided. The Committee was told that, generally, time series data are not routinely collected for that purpose. Notwithstanding, the Committee heard that these data could be used to determine if the services being provided were improving or getting worse but would need to be collected on a resident mix adjusted basis as well as a case mix adjusted basis.<sup>17</sup>
- 2.36 According to Health there had been a change from using an input model (which measured services provided) to the adoption of an output model (which measured achievements). Health said that this approach had been undertaken to improve the consistency of the assessments of the many aspects of the aged care industry. Adoption of the output model also ensured that a single system applied right across the whole industry. Nevertheless there was still a need for balance between subjectivity and objectivity.<sup>18</sup>
- 2.37 *Clinical quality* measures of resident care, such as number of falls, restraint and infection controls, should be augmented by social engagement measures such as residents talking to people and engaging with staff.<sup>19</sup> A bland statistical approach (such as numbers of events and whether medicine arrives on time) tended to obscure the fact that there were distinct sub-groups in high care populations. Further, such an approach tended not to record *quality-of-life* issues.

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17 The Agency, *Transcript, 18 August 2003*, p. 5.

18 Health, *Transcript, 18 August 2003*, p. 8.

19 Health, ACSA, *Transcript, 18 August 2003*, pp. 8-9.

- 2.38 The Committee raised as an important issue, whether the quality of aged care had improved as a result of the accreditation process which has now proceeded beyond the second round. It noted that accreditation had gone well but queried whether there were any measures indicating that the residents' *quality-of-life* had improved.
- 2.39 ACSA responded that there were processes that could amount to proper benchmarking between countries, and over time. However, data of the nature required were not currently readily available at present.<sup>20</sup>
- 2.40 Since the introduction of accreditation, every home receiving Commonwealth funds had been seen by the Agency and measured against a set of outcomes.<sup>21</sup> Certification and accreditation had meant that a culture of continuous improvement had been imbued in the industry, according to the Australian Nursing Homes and Extended Care Association (ANHECA). Indeed some homes had left the industry at the commencement of accreditation and those that remain were committed to improving services. The accreditation process was more robust and independent and the focus was now on quality systems.<sup>22</sup>
- 2.41 ACSA suggested that there were strong reasons for "a more open approach [towards the process of accreditation] because the majority of our members do more than one thing".<sup>23</sup> A less rigid approach would open up the opportunity to employ benchmarking practices used in other community care industries. ACSA believed there should be a number of accreditation service providers operating under the Joint Accreditation System of Australia & New Zealand (JAS-ANZ) framework. Further, the aged care facility operators may also have as many as a dozen other types of services or streams that require accreditation. These may include a more comprehensive range of services to older people, as well as perhaps disability services, in total requiring around six different accreditations. Hence, it was argued, it was possible for one accrediting team to do all a particular company's accreditations in one campaign.<sup>24</sup>
- 2.42 An estimated 600 of the 3000 aged care facilities facing accreditation undertook voluntary benchmarking for their clinical services. This assisted the efficiency of the accreditation process because,

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20 ACSA, *Transcript, 18 August 2003*, p. 5.

21 Health, *Transcript, 18 August 2003*, p. 13.

22 Australian Nursing Homes and Extended Care Association (ANHECA), *Transcript, 18 August 2003*, p. 15.

23 ACSA, *Transcript, 18 August 2003*, p. 6.

24 ACSA, *Transcript, 18 August 2003*, p. 6; ACSA, *Submission No. 1*, pp. 2-4.

...when assessors visit facilities which have those sorts of systems in place, they use them extensively to demonstrate the quality improvement framework.

As people see that it assists their accreditation process quite specifically and demonstrably, that assistance and take-up rate will grow.<sup>25</sup>

- 2.43 The Committee was advised by ACSA that the JAS-ANZ<sup>26</sup> (the body that sanctions accreditation agencies) had developed a set of criteria for accreditation,<sup>27</sup> and hence a mechanism for accrediting the accreditors was in place. ACSA contended that,

...placing accreditation for aged care services under an open accountability framework such as JAS-ANZ would be the best way of ensuring that the concerns and issues identified by ANAO are addressed for now and into the future.<sup>28</sup>

### Committee comment

- 2.44 Notwithstanding the evidence presented to it, the Committee feels that there is scope for variations to exist in assessments without invalidating the assessments themselves. The Committee believes also that reasonable progress is being made on quality and reliability of accreditation services provided by the Agency.
- 2.45 The Committee finds compelling ACSA's argument that over-arching JAS-ANZ certification of the Agency as an accreditation body ensures that the Agency's systems remain robust. The possibility of collateral benefits to the broader community care sector warrant review by Health.
- 2.46 The Committee notes that the areas where improvements can be made to the *clinical quality* of aged care have been adequately identified. However, the Committee recognises that the *quality-of-life* experienced by the residents of aged care homes is more difficult to characterise and measure objectively, and hence this aspect appears not to have been factored into the overall accreditation process in a meaningful way.
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25 ANHECA, *Transcript, 18 August 2003*, p. 7; ANHECA, *Submission No. 2*, p. 30.

26 JAS-ANZ Committee was established in 1991 by a formal agreement between the Governments of Australia and New Zealand. It has the legal status of an International Organisation. It assesses and accredits personnel, systems and products. The principal advantage of using a JAS-ANZ accredited certification body is that it has demonstrated it uses competent and impartial personnel in all stages of its auditing and certification process. ANHECA, *Submission No. 2*, pp. 31-6.

27 ACSA, *Transcript, 18 August 2003*, p. 17.

28 ACSA, *Submission No. 1*, p. 4.

- 2.47 The Committee finds that, despite all the effort and cost to date in implementing accreditation, the Agency's current system of accreditation tells little about whether the quality-of-life of people in aged care facilities *has actually improved*. The Committee concludes therefore that a better mechanism for assessing quality-of-life for residents in aged care facilities needs to be developed, without imposing additional costs on the aged care facilities or further complicating the accreditation process. Clinical quality data need to be complemented by quality-of-life data possibly including impressions gained during interviews by accreditors with residents, their families and visitors. The Committee recommends accordingly.

### Recommendation 1

- 2.48 **The Aged Care Standards and Accreditation Agency Limited broaden the focus of the quality assessment data currently used for accreditation purposes, to include quality-of-life information experienced industry-wide by residents of aged care homes. Overall, the resultant data collection mechanism must not impose additional costs on the aged care facilities nor further complicate the accreditation system.**

## Costing methodology

- 2.49 ANAO found that the Agency employed a "suspect system" to cost its services – its costing methodology did not embrace time sheet usage, and the Agency was still in the process of establishing a system to monitor budget variances.
- 2.50 the Agency explained that its costing model involved three stages, the first two of which were in place:
- Budget estimates;
  - Expensing according to function; and
  - Budget validation.
- 2.51 The volatility of the financial results reported by the Agency, whereby significant losses were made in the years between the accreditation peaks, was of concern to the Committee. The Agency explained that generally it operated at a loss for two years and then in the third year, recorded an operating profit. Negotiating "certainty of funding" from Health, rather

than a particular appropriation would allow the Agency to achieve long term solvency.<sup>29</sup>

### **Committee comment**

- 2.52 The Committee is concerned that the Agency's revenue flow is highly volatile. It concludes, however, that considering the cyclical nature of the workload, and with the accreditation process having only just completed its second round, it is not realistically possible, at this stage, to achieve a uniform revenue flow. Nevertheless the Committee is encouraged that processes are being put in place by the Agency to ensure rigorous cost supervision.

### **Training of nurses**

- 2.53 The Committee investigated whether there was sufficient emphasis on aged care skills training in the academic courses that nurses were required to undertake to gain their nursing accreditation,
- 2.54 ACSA advised the Committee that there were significant variations in the content of nursing training across Australia, in terms of time and content on aged care and indeed, on processes such as accreditation. On this basis there was a need to base training on quality of service rather than strictly aged care. Pressures on maintaining quality of aged care were exacerbated by a shortage of nurses. Therefore, any steps aimed at improving the quality of care needed to take into account the resources actually available, not some desired but ultimately unrealistic resourcing level.<sup>30</sup>

### **Committee comment**

- 2.55 The Committee accepts that resourcing constraints exist, particularly with respect to overall nurse numbers, but it considers that academic institutions providing nursing training need to include in their curricula adequate levels of training specifically relating to aged care.

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29 The Agency, *Transcript, 18 August 2003*, p. 11.

30 ACSA, *Transcript, 18 August 2003*, p. 15.

## **Facility ownership**

- 2.56 The Committee questioned whether ownership of aged care facilities – not-for-profit, private, state, or municipal – had any impact on quality of care.
- 2.57 The Committee was advised that data that could be used to determine whether quality of aged care varied according to the nature of facility ownership, were not available. The Committee suggests that some research by Health is warranted, to determine if the nature of facility ownership affects quality of aged care.





## Audit Report No. 51, 2002–03

# Defence Housing and Relocation Services

## Introduction

### Background

- 3.1 The Department of Defence (Defence) has long provided housing assistance for members of the Australian Defence Force (ADF) and their families. The Defence Housing Authority (DHA) was established in 1988 to provide suitable housing to meet operational needs of Defence. DHA became a Government Business Enterprise (GBE) in 1992. In response to the Government's desire that DHA operate more commercially, provision of housing was formalised in 2000, when Defence and DHA signed a Services Agreement. Defence remains responsible for setting housing standards and for overall management of housing and relocations assistance for ADF.
- 3.2 The Government considers that providing high-quality accommodation is essential if ADF is to retain members. DHA has done much to improve housing for members and their families. DHA surveys of ADF tenants indicate a high degree of customer satisfaction with their housing.<sup>1</sup>

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1 Australian National Audit Office (ANAO), Report No. 51, 2002–03, *Defence Housing and Relocation Services*, p. 11.

- 3.3 During 2000 and 2001 DHA began providing Defence with housing related services. These were formalised in the Relocations Service Agreement; a second agreement signed in 2002. Services provided by DHA include:
- arranging housing allocation and relocation;
  - arranging for Defence to make payment of Rent Allowance to members to use private houses;
  - arranging payment of relocation and temporary accommodation allowances (on a reimbursement basis); and
  - arranging end-of-tenancy cleaning of service residences.

## The Audit

- 3.4 The ANAO audit began in July 2002. It assessed whether Defence's management of its housing and relocation service provided for ADF members meets specified requirements; and made practical recommendations for more efficient, effective and economical use of public resources provided for this purpose.
- 3.5 A focus of the audit was on Defence's preparation for, and management of, the \$3.5 billion 10-year Services Agreement between Defence and DHA, which was signed in 2000. It is one of Defence's largest service delivery arrangements.

## Audit Findings

- 3.6 ADF members and their families acknowledge the quality of the housing they receive under Defence housing arrangements. Defence aims to maintain a high satisfaction rate among members and their families in respect of those arrangements. However, the audit report noted that Defence should also aim to monitor and contain the associated costs. With a focus on member satisfaction, the standard of housing provided exceeds Defence's specified requirement. Defence has largely accepted this outcome, in spite of rising cost of housing and related services, which in 2001-02 amounted to some \$594 million.
- 3.7 ANAO was critical of the 2000 Services Agreement between Defence and DHA. ANAO considered that it would have been preferable had Defence properly constructed the commercial contract and acted on legal advice that the Agreement would not adequately protect Defence's interests. ANAO believed that Defence did not sufficiently appreciate that DHA was not a part of the Department of Defence, but rather was a GBE that

provided housing services on a commercial basis and as an entirely separate and independent entity.

- 3.8 This underlined a need for Defence to manage arrangements strategically and ensure that services met requirements and provided value for money. Defence also needed to implement the Service Agreement's provisions for programs of continuous improvement and cost control.
- 3.9 ANAO detailed its concerns in the following areas:
- the need to formalise the service arrangements;
  - the requirement for more effective strategic and operational management of the services;
  - the need to clarify and finalise several outstanding issues with the performance management of the services; and
  - the need to develop a more proactive approach to the financial management of the services.
- 3.10 The audit report made five recommendations to Defence. These included considering a review of the provision in the *Defence Housing Authority Act 1987* (DHA Act) for Defence officers to be appointed to the DHA board, and working to complete action on significant transitional issues. Other recommendations addressed the Defence annual housing forecast, visibility of housing assistance financial decisions and the payment process for DHA invoices. Defence agreed to four Recommendations without qualification and one Recommendation with qualifications.

## The Committee's Review

- 3.11 On 15 September 2003 the Committee held a public hearing to review the progress made against the audit's recommendations. The public hearing was attended by:
- Australian National Audit Office;
  - Department of Defence; and
  - Defence Housing Authority.

3.12 The Committee took evidence on the following issues:

- the Service Agreement;
- composition of the DHA board;
- vacant housing;
- the quality maintenance fee; and
- outstanding issues.

## The Service Agreement

3.13 DHA's duty to provide housing services to Defence is set out in a Service Agreement titled *Services Agreement for Housing and Related Requirements*. This Service Agreement was signed in August 2000, and was developed in response to a recommendation of ANAO's Audit Report No. 13, 1994-95, *Australian Defence Force Housing Assistance*.<sup>2</sup>

## The nature of the Service Agreement

3.14 Concerns were expressed by ANAO over the non-businesslike manner in which the Service Agreement was struck.<sup>3</sup>

3.15 The DHA shareholder Ministers<sup>4</sup> requested in 1999 that the Service Agreement cover the allocation of risk associated with commercial and service delivery operations.<sup>5</sup> In April 2000, the shareholder Ministers stated that this should be achieved by creating a Service Agreement that was a commercial contract. In a letter sent to DHA, the Ministers stated:

...the Agreement must be a properly constructed commercial contract, reflecting in an unambiguous manner the risks and obligations of each party.<sup>6</sup>

3.16 DHA, however, felt that a commercial contract was unnecessary to achieve the proper allocation of risks, as the DHA Act obliges DHA to operate with a commercial allocation of risks.<sup>7</sup>

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2 ANAO, Report No. 51, 2002-03, *Defence Housing and Relocation Services*, p. 30.

3 ANAO, Report No. 51, 2002-03, *Defence Housing and Relocation Services*, pp. 37-8.

4 The Defence Housing Authority (DHA) is responsible to two shareholder Ministers: the Minister for Defence and the Minister for Finance and Administration.

5 ANAO, Report No. 51, 2002-03, *Defence Housing and Relocation Services*, pp. 30-1.

6 ANAO, Report No. 51, 2002-03, *Defence Housing and Relocation Services*, p. 32.

7 ANAO, Report No. 51, 2002-03, *Defence Housing and Relocation Services*, p. 32.

- 3.17 In May 2000, Defence indicated its acceptance of DHA's view that a commercial contract was not required. Defence stated that an agreement that was not a commercial contract would be sufficient to satisfy the shareholder Ministers' requirements for the allocation of risks.<sup>8</sup>
- 3.18 The Service Agreement, in this form, was approved by the shareholder Ministers on the understanding that appropriate measures were in place to deal with the business and other risk issues.<sup>9</sup>
- 3.19 DHA told the Committee a commercial contract was not the primary goal of the shareholder Ministers.
- ...the requests from ministers were wider than just a commercial agreement. ... DHA was created in 1998 and it operated until... 2000 without a formal agreement between [Defence] and the organisation. Secondly, what ministers were on about was an agreement that specified risk-sharing. They wanted the arrangement to be transparent so that there were the right price signals.<sup>10</sup>
- 3.20 Defence advised the Committee that, in its view, it was unnecessary for the Service Agreement to be a commercial contract. It reasoned that such a contract would never be disputed in court because both Defence and DHA are owned by the Commonwealth. Instead, any disputes would be resolved by ministerial negotiation.
- [I]s this a real contract? For example, would these two parties ever end up in a court of law? Well, I would have the thought the answer to that is probably no—because, in the finish, ministers would pull us into line.<sup>11</sup>
- 3.21 ANAO noted that DHA was required by the DHA Act to operate commercially, but that Defence had a responsibility to act in a business-like manner also. ANAO suggested that Defence should have done more to apply the principles of “value for money” and “open and effective competition” in its dealings with DHA. This would have involved Defence analysing the proposed DHA charges and comparing them with those that another provider might charge in similar circumstances.<sup>12</sup>

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8 ANAO, Report No. 51, 2002–03, *Defence Housing and Relocation Services*, p. 32.

9 ANAO, Report No. 51, 2002–03, *Defence Housing and Relocation Services*, pp. 36-7.

10 DHA, *Transcript*, 15 September 2003, p. 7.

11 Department of Defence (Defence), *Transcript*, 15 September 2003, p. 4.

12 ANAO, Report No. 51, 2002–03, *Defence Housing and Relocation Services*, p. 33.

- 3.22 ANAO deemed these comments sufficient and did not make a recommendation on the nature of the Service Agreement.

### Committee comment

- 3.23 The Committee concedes that a strictly commercial contract is not necessary to ensure that risks and obligations are properly distributed. The Committee believes, however, that Defence has a responsibility to act in a business-like manner in its dealings with DHA to ensure that Defence receives value for money and protects its own interests.

### Legal advice

- 3.24 During the drafting of the Service Agreement, Defence sought legal advice on the termination clause. In June 2000 Defence was advised of significant legal and practical concerns with the clause that could lead to long-term detriment to the Commonwealth. Of greatest concern was that Defence seemed to have no ability to terminate the Service Agreement for default by DHA.<sup>13</sup>
- 3.25 Defence did not act on the legal advice. The termination clause in the draft Service Agreement was not amended and no other clause was inserted to address these concerns.<sup>14</sup>
- 3.26 Defence told ANAO that the legal advice was not applicable to the relationship between DHA and Defence. It stated that the absence of a contractual termination for default provision was not critical because of protection provided by the DHA Act. The DHA Act obliges DHA to provide Defence with adequate housing and holds it subject to the direction of the Minister. Further, the Agreement includes a dispute mechanism which provides for binding arbitration. These protections meant that it was not necessary, in the view of Defence, to alter the termination clause of the Agreement.<sup>15</sup>
- 3.27 The legal advice was received by a senior Defence officer acting as contract authority, who did not pass it on to the Secretary of Defence or the shareholder Ministers. The contract authority informed the Secretary of some aspects of legal advice, but did not include the advice that the

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13 ANAO, Report No. 51, 2002–03, *Defence Housing and Relocation Services*, p. 34.

14 ANAO, Report No. 51, 2002–03, *Defence Housing and Relocation Services*, p. 34.

15 ANAO, Report No. 51, 2002–03, *Defence Housing and Relocation Services*, p. 34.

Agreement would not adequately protect Defence's interests and would involve serious risks for Defence.<sup>16</sup>

- 3.28 Defence told the Committee that the Secretary was given a summary of the legal advice, but was not given details for reasons of brevity.

The concerns about the nature of the contract were drawn to the attention of the Secretary of the department. I would have to say that, if the details of legal opinions on every contract—albeit a very important contract—that the department signs were provided to the Secretary, his in-tray would become even more overloaded than it is at present. ... So the concerns were summarised in the advice that went to the Secretary.<sup>17</sup>

- 3.29 Defence also told the Committee that the Secretary did not seek further advice on the basis of the information presented to him.<sup>18</sup>

- 3.30 ANAO stated that the contract authority should have better informed the Secretary of Defence and shareholder Ministers of the extent of the legal advice so that they could also apply their experience and judgment to the issues presented in order to better protect the Commonwealth's interests at the time.<sup>19</sup>

### Committee comment

- 3.31 The Committee believes that the Secretary and shareholder Ministers should have been better informed about the legal advice expressing concerns that the agreement might not safeguard Defence objectives, especially given that the legal advice has not been followed. While the relationship between DHA and Defence might ultimately be governed by the DHA Act, the Service Agreement should still be as robust and comprehensive as possible while being consistent with the DHA Act. For this reason, the termination clause in the Service Agreement should be legally sound and unambiguous.

### Conflicting objectives

- 3.32 The Committee is concerned that the commercial nature of the Service Agreement has led to a conflict of objectives between Defence and DHA. Defence requires high-quality, cost-effective housing for its members

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16 ANAO, Report No. 51, 2002–03, *Defence Housing and Relocation Services*, pp. 35, 38.

17 Defence, *Transcript*, 15 September 2003, p. 3.

18 Defence, *Transcript*, 15 September 2003, pp. 3-4.

19 ANAO, Report No. 51, 2002–03, *Defence Housing and Relocation Services*, p. 38.

while DHA is required to increase its rate of return. These objectives encourage DHA to supply higher-quality housing than is required by Defence.

- 3.33 Defence requirements specify that all service residences have basic amenities, plus additional amenities according to the rank of the resident. Service residences are divided into six classifications (A, B1, B2, C, D and E) according to how many additional amenities they have.<sup>20</sup> The higher the grade, the higher the cost to Defence. The greatest numerical need is for Grade A housing, which are two bedroom houses with no additional amenities.<sup>21</sup>
- 3.34 DHA is a commercial agency, and must be cost-effective in its provision of housing. The most cost-effective way to obtain housing is to lease it from private investors. The private investor market supplies relatively few two bedroom houses. Most private investor houses have four bedrooms.
- ...the typical house in the market that we can put on the sale-and-leaseback program because of the prospects of capital growth for the investor tends to be about a four-bedroom house. That is typically what you will see if you go into any housing development.
- If we come to the point in relation to... [Group A] houses, they are houses that do not have en suites or family rooms. The markets stopped producing those sorts of houses quite some time ago.<sup>22</sup>
- 3.35 ADF personnel may be allocated housing that is one grade above their entitlement if no housing of the entitled grade is available. In this case, they pay rent according to their entitled grade and Defence makes up the difference.<sup>23</sup> Therefore, it costs Defence more if DHA is unable to provide housing in the required grades.
- 3.36 The audit report stated that DHA was reducing its stock of Group A houses and replacing them with higher classification houses. This is increasing Defence costs when DHA is unable to provide Defence with the required number of Group A houses.<sup>24</sup>

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20 ANAO, Report No. 51, 2002–03, *Defence Housing and Relocation Services*, p. 22.

21 ANAO, Report No. 51, 2002–03, *Defence Housing and Relocation Services*, p. 74.

22 DHA, *Transcript*, 15 September 2003, p. 5.

23 ANAO, Report No. 51, 2002–03, *Defence Housing and Relocation Services*, p. 77.

24 ANAO, Report No. 51, 2002–03, *Defence Housing and Relocation Services*, pp. 75-6.



- 3.37 ANAO agreed with the Committee's observation that this situation indicates a conflict of objectives.<sup>25</sup>
- 3.38 Both Defence and DHA said that they believed that their aim was to provide satisfactory or better housing, and this was best achieved by operating DHA on a commercial basis.<sup>26</sup>
- 3.39 Defence advised the Committee that it considered this situation to be acceptable because it is only temporary. Defence said it was in the process of developing a new housing classification to suit the current housing market and occupant expectations. This will mean that DHA can cost-effectively provide more housing in the lowest grade, and more ADF personnel can be allocated housing of the correct grade. The new classification will change the type of housing required by Defence, but will not affect its objectives of providing satisfactory, low-cost housing.<sup>27</sup>
- 3.40 Defence also told the Committee that the situation was a compromise between cost and personnel retention. It costs more to provide better than satisfactory housing, but this encourages ADF personnel to stay in the Australian Defence Force.

I mean, if you doubled my salary, I might be more likely to stay on until I am 65. If you doubled the size of all houses and the salaries for the ADF, you would retain a higher proportion of them. We have to make judgments. If houses are not consistent with, or within cooee of, community standards, that will be an issue in terms of retention. So there has to be a trade-off here. I would not call it a conflict.<sup>28</sup>

### Committee comment

- 3.41 The Committee acknowledges that Defence and DHA both have interests in providing satisfactory, cost-effective housing to ADF personnel.
- 3.42 The Committee understands that the current Defence requirement for Grade A housing is a product of its housing classification, and is not fundamental to its objectives of providing satisfactory, cost-effective housing. The Committee recognises that there may be no cost-effective way to provide Defence with sufficient Grade A housing as it is currently defined.

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25 ANAO, *Transcript, 15 September 2003*, p. 5.

26 Defence, *Transcript, 15 September 2003*, p. 4; DHA, *Transcript, 15 September 2003*, p. 4.

27 ANAO, Report No. 51, 2002–03, *Defence Housing and Relocation Services*, p. 79; Defence, *Transcript, 15 September 2003*, p. 18.

28 Defence, *Transcript, 15 September 2003*, p. 6.

- 3.43 The Committee expects that Defence's new housing classification should reduce defence housing costs by reducing the number of personnel placed in housing rated above their respective entitlements. However, while the new housing classification may reflect the current housing market supply, the housing market supply may still change again in the future. The Committee encourages Defence to implement more flexible housing classifications that can match economically the changing nature of the housing market and occupant expectations.

## Composition of the DHA board

- 3.44 Under the DHA Act, the DHA board has 12 members; three of which are ADF members.<sup>29</sup> Currently the board includes four ADF members and one civilian Defence official.<sup>30</sup>
- 3.45 The audit report pointed out that because DHA is now a GBE, the presence of Defence officers on the DHA board creates a potential conflict of interest. The board must take business decisions in the interests of DHA and also take a commercial approach to Defence. Accordingly, ANAO recommended that Defence review the provisions in the DHA Act for Defence officers to be appointed to the DHA board. Defence has agreed to this recommendation, but DHA disputes the assertion that there is a potential conflict of interest.<sup>31</sup>
- 3.46 DHA told the Committee that, even before it became a GBE, there had been potential for conflicts of interest. This was because the board also included commercial directors, and arrangements existed to deal with conflicts of interest.<sup>32</sup> The DHA Act requires board members to disclose their interests in matters being considered by DHA.<sup>33</sup>
- 3.47 DHA explained to the Committee that the DHA board believes that having Defence officers among its members helps ensure the provision of quality housing services. Defence was an important stakeholder in DHA operations, and it was important that its requirements be known to the DHA board. If Defence officers were removed from the DHA board, then

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29 *Defence Housing Authority Act 1987*, Section 12 (1).

30 ANAO, Report No. 51, 2002–03, *Defence Housing and Relocation Services*, p. 25.

31 ANAO, Report No. 51, 2002–03, *Defence Housing and Relocation Services*, pp. 49–50.

32 DHA, *Transcript*, 15 September 2003, p. 14.

33 *Defence Housing Authority Act 1987*, Section 20.

the board would recommend the implementation a formal advisory arrangement to represent Defence interests.<sup>34</sup>

- 3.48 The audit report states that DHA has other means of learning of Defence requirements, including representation on two bodies established by the Service Agreement. The Defence Domiciliary Group (DDG), a high level strategic management body, monitors and reviews the Service Agreement and sets terms of reference for that monitoring. The Domiciliary Operations Committee (DOC) supervises the operations of the Service Agreement at a national level.<sup>35</sup>

### Committee comment

- 3.49 Good corporate governance requires that boards have in place arrangements to avoid even the perception that their members may face regular conflicts of organisational influence. The *Commonwealth Authorities and Companies Act 1997* (CAC Act) requires directors of a CAC authority board to make business judgements in the best interests of the authority.<sup>36</sup> DHA is a CAC authority, and ADF members of its board may face a potential conflict of interest if the board discusses commercial decisions that are in the interests of DHA but not in the interests of Defence.
- 3.50 ANAO has recommended that Defence consider reviewing and providing advice to the Government on the provision in the DHA Act for Defence officers to be appointed to the DHA board.<sup>37</sup> The Committee wishes to go one step further and recommends that the provision for ADF members to be appointed to the DHA board be removed from the DHA Act.
- 3.51 At the same time, the Committee acknowledges the importance of the advice that ADF members can give the DHA board. For this reason, the Committee believes that this amendment to the DHA Act be accompanied by changes to the Service Agreement to strengthen the advisory role of DDG.

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34 DHA, *Transcript*, 15 September 2003, pp. 14-5.

35 ANAO, Report No. 51, 2002-03, *Defence Housing and Relocation Services*, pp. 50-1.

36 *Commonwealth Authorities and Companies Act 1997*, Section 22.

37 ANAO, Report No. 51, 2002-03, *Defence Housing and Relocation Services*, p. 50.

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## Recommendation 2

- 3.52 **Section 12 (1) of the *Defence Housing Authority Act 1987* be amended to remove the provision that the Defence Housing Authority include three members of the Australian Defence Force.**

**The *Services Agreement for Housing and Related Requirements* be amended to allow for a formal consultative process, possibly including the Defence Domiciliary Group, to enable the Department of Defence to advise Defence Housing Authority of Australian Defence Force housing requirements.**

## Vacant housing

- 3.53 Defence and DHA pay rent on unoccupied defence housing. Under the Service Agreement, Defence was responsible for pre-disposal vacancy charges for housing that it decided was no longer required, and DHA was responsible for inter-tenant vacancies.<sup>38</sup>
- 3.54 In practice, Defence is responsible for the cost of the first three months of inter-tenant vacancies, and DHA for the cost after three months.<sup>39</sup>
- 3.55 DHA told the Committee that some vacancies were unavoidable because it needed to ensure that houses were available for the peak posting period.<sup>40</sup>
- 3.56 The number of housing vacancies had been exacerbated by a large reduction in the housing requirement since 1999.<sup>41</sup>
- 3.57 DHA told the Committee that ADF personnel could vacate Defence housing on short notice, and that this was responsible for some of the vacant housing, but that a policy was in place to deal with this situation.

We are operating in an environment where [ADF personell]... can buy their own house and move out with almost no notice at all.

We have this policy of either disposing of the stock or putting civilian tenants in it as quickly as possible. Indeed, we have

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38 ANAO, Report No. 51, 2002–03, *Defence Housing and Relocation Services*, p. 79.

39 ANAO, Report No. 51, 2002–03, *Defence Housing and Relocation Services*, pp. 79-80; DHA, *Submission No. 3*, p. 2.

40 DHA, *Transcript, 15 September 2003*, p. 16.

41 DHA, *Submission No. 3*, p. 13; ANAO, Report No. 51, 2002–03, *Defence Housing and Relocation Services*, p. 14.

substantial numbers of civilian tenants now in our stock as a means to deal with vacancies.<sup>42</sup>

- 3.58 DHA also noted that the average turnover, between one tenant moving out and another moving in, was about thirty days.<sup>43</sup>
- 3.59 DHA has made some progress in reducing the number of vacant houses. Since 1999, when it assumed responsibility for housing allocation, the percentage of DHA houses that were vacant fell from 9.5% to 8.6%. The elimination of over 500 vacant houses has resulted in annual savings of approximately \$7 million.<sup>44</sup>
- 3.60 DHA told the Committee that it has implemented a system to reduce the cost of inter-tenant vacancy by reducing the requirement for temporary accommodation. The HomeFind tool helps ADF personnel to choose a property in their new posting location in advance, allowing them to relocate from door to door. This has resulted in substantial savings.<sup>45</sup>
- 3.61 DHA also advised the Committee that it was not feasible to reduce inter-tenant vacancy costs by passing them on to the housing market. A typical DHA property lease has a nine year term, but Defence required that ADF personnel be able to terminate a housing contract with ten days notice. Inter-vacancy costs could be reduced by negotiating leases on the same terms, but these terms would be unacceptable to private housing investors.<sup>46</sup>
- 3.62 Defence also informed the Committee that it was willing to negotiate with DHA to create a formal cost reduction program.<sup>47</sup>

### Committee comment

- 3.63 The Committee is pleased to note DHA's efforts to reduce the cost of housing vacancies, both to itself and to Defence, and will follow with interest the efforts of Defence and DHA to create a formal cost reduction program.

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42 DHA, *Transcript, 15 September 2003*, pp. 16-7.

43 DHA, *Transcript, 15 September 2003*, p. 17; DHA, *Submission No. 3*, p. 13.

44 DHA, *Submission No. 3*, pp. 10, 13.

45 DHA, *Transcript, 15 September 2003*, p. 17; DHA, *Submission No. 3*, p. 13.

46 DHA, *Transcript, 15 September 2003*, p. 8.

47 Defence, *Transcript, 15 September 2003*, pp. 17-8.

## The quality maintenance fee

- 3.64 The Committee examined several aspects of the costs that DHA incurs of Defence. The most significant of these was the quality maintenance fee.
- 3.65 DHA charges Defence a quality maintenance fee on Defence housing. The audit report stated that Defence was being charged twice for a service that was already covered by rental fees. ANAO estimated that as a result, Defence paid an additional \$1.7 million in 2001–02 and a similar amount in 2000–01. However, this issue was not considered when the Service Agreement was negotiated.<sup>48</sup>
- 3.66 DHA told the Committee that the quality maintenance fee was not a double charge. DHA provides ADF personnel with a maintenance service that was superior to that offered by the private housing market, including a 24-hour helpline and providing for the booking of contractors to turn up at agreed times. This higher level of service incurred a higher cost and necessitated the quality maintenance fee.<sup>49</sup>

### Committee comment

- 3.67 The Committee accepts that the quality maintenance fee is not a double charge, and that it is necessary to provide such a high level of service.
- 3.68 However, the quality maintenance fee may be a potential source of savings, and Defence and DHA should consider the level of maintenance service that balances the expectations of ADF tenants and the cost to Defence.

## Outstanding issues

- 3.69 The audit report stated that a list of ten outstanding issues between Defence and DHA had been brought to the attention of the DHA board before the signing of the Service Agreement. Eight of these issues were to be resolved within three months of the signing of the Service Agreement. At the time of the audit, more than two years later, four of these issues had not been resolved.<sup>50</sup>

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48 ANAO, Report No. 51, 2002–03, *Defence Housing and Relocation Services*, p. 86.

49 DHA, *Transcript*, 15 September 2003, p. 20.

50 ANAO, Report No. 51, 2002–03, *Defence Housing and Relocation Services*, pp. 59-60.

- 3.70 Defence told the Committee that these delays were not acceptable, and that Defence was making progress against these issues by reviewing the management framework of the Service Agreement. The audit report revealed deficiencies in this framework. Once these deficiencies were rectified, Defence indicated that it would work with DHA to address the outstanding issues.<sup>51</sup>
- 3.71 Defence told the Committee of its progress against the following outstanding issues:
- Continuous Improvement Program;
  - Key Performance Indicators;
  - Property register; and
  - Review of deemed effective markets.
- 3.72 The Service Agreement provided for DHA to develop a **Continuous Improvement Program** in order to reduce the cost of the Defence rent bill. Defence records indicated that DHA was developing such a program in August 2000 to target the areas of “dead rent”, temporary accommodation, storage, travel costs, mismatches and ADF retention. There has been no progress on these issues, and there was no evidence of a Continuous Improvement Program. Defence told the Committee that it has not yet conferred with DHA on how to reduce Defence housing costs.<sup>52</sup>
- 3.73 The Service Agreement provides for **Key Performance Indicators** that measure:
- the general satisfaction of Defence families;
  - the overall cost to Defence;
  - the meeting of specifications in terms of services and accommodation;
  - the administration of payments; and
  - the sharing of risks.<sup>53</sup>
- 3.74 Detailed Key Performance Indicators were proposed in December 2000, but there was no evidence that they were finalised and implemented.

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51 Defence, *Transcript, 15 September 2003*, p. 9.

52 ANAO, Report No. 51, 2002–03, *Defence Housing and Relocation Services*, pp. 62-4; Defence, *Transcript, 15 September 2003*, p. 9.

53 ANAO, Report No. 51, 2002–03, *Defence Housing and Relocation Services*, p. 64.

Defence told the Committee that a set of indicators proposed by DHA was currently going through the Defence committee process.<sup>54</sup>

- 3.75 ANAO could not determine whether the DHA **property register** for July 2000 was checked for accuracy by Defence. Defence records noted that the initial register, detailing classifications for all stock, to be agreed by both parties by 30 June 2000, “did not occur”. Defence told the Committee that DHA was now providing Defence with an updated property register every six months.<sup>55</sup>
- 3.76 The Service Agreement states that Defence and DHA will review, “by 28 February 2001”, the classification of **deemed effective markets**.<sup>56</sup> This review has not taken place. Defence pays DHA an annual premium for the properties in this “market”. This premium was to be transitional and not to extend beyond the first year if agreement was reached. Current effective markets, where Defence pays this premium, include Canberra, Brisbane and Adelaide. Defence told the Committee that it intended to engage an independent authority to review these markets.<sup>57</sup>
- 3.77 The audit report noted that the outstanding issue of Housing Management Instructions was still in draft form, but was operational.<sup>58</sup> Defence explained to the Committee that Housing Management Instructions are a set of agreed definitions and responsibilities that allow it to know the full cost of the rent bill. Defence considers Housing Management Instructions to be the best way of defining responsibilities and liabilities under the Service Agreement.<sup>59</sup>

### Committee comment

- 3.78 The Committee notes the progress against the outstanding issues identified in the audit report, but is concerned at the amount of time required by Defence to come this far.

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54 ANAO, Report No. 51, 2002–03, *Defence Housing and Relocation Services*, p. 64; Defence, *Transcript, 15 September 2003*, p. 9.

55 ANAO, Report No. 51, 2002–03, *Defence Housing and Relocation Services*, p. 60; Defence, *Transcript, 15 September 2003*, p. 9.

56 An **effective market** is one where charges to Defence are primarily based on local market rental values. The alternative is a **limited market**, where charges to Defence are formulated to recoup the capital value of the property and generate a commercial rate of return for DHA. All on-base houses are treated as a limited market.

57 ANAO, Report No. 51, 2002–03, *Defence Housing and Relocation Services*, p. 60; Defence, *Transcript, 15 September 2003*, p. 9.

58 ANAO, Report No. 51, 2002–03, *Defence Housing and Relocation Services*, p. 60.

59 Defence, *Transcript, 15 September 2003*, p. 10.



**Recommendation 3**

- 3.79 **The Department of Defence report within six months to the Joint Committee of Public Accounts and Audit on its progress towards addressing the outstanding issues listed in Paragraph 4.6 of the Australian National Audit Office Audit Report No. 51, 2002–03, *Defence Housing and Relocation Services*.**



## Audit Report No. 55, 2002–03

# Goods and Services Tax Fraud Prevention and Control

## Introduction

### Background

- 4.1 Fraud against the Commonwealth is a major concern to the Government. Agencies must ensure that fraud is minimised and, where fraud does occur, is rapidly detected, effectively investigated, appropriately prosecuted, and losses minimised.<sup>1</sup>
- 4.2 The Commonwealth Fraud Control Guidelines (Fraud Control Guidelines) require Commonwealth agencies to put in place a comprehensive fraud control program that includes prevention, detection, investigation and reporting strategies. The Guidelines, which define fraud as *dishonestly obtaining a benefit by deception or other means*—include both tangible and intangible benefits and apply to all agencies covered by the *Financial Management and Accountability Act 1997* (the FMA Act) and bodies covered by the *Commonwealth Authorities and Companies Act 1997* that receive at least 50% of their funding for operating costs from the Commonwealth.

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1 Attorney-General's Department (AGD), *Commonwealth Fraud Control Guidelines*, p. iii.

- 4.3 The Attorney-General's Department (AGD), the Australian Federal Police (AFP) and the Commonwealth Director of Public Prosecutions (DPP) are the Commonwealth agencies with cross-government responsibilities in relation to fraud control. In short AGD advises, AFP investigates and DPP prosecutes.
- 4.4 The Australian Taxation Office (ATO) function is to manage and shape the revenue systems that give effect to social and economic policy, and fund government services for Australians. Its response to fraud complies with the FMA Act.
- 4.5 Introduced from 1 July 2000, the Goods and Services Tax (GST) is a broad-based indirect tax, imposed on goods and services at each point in the distribution chain, including at importation. GST replaced the existing wholesale sales tax and a number of indirect state taxes. The GST rate is 10 per cent.

## The Audit

- 4.6 The audit by Australian National Audit Office (ANAO) assessed whether ATO has implemented administratively effective GST fraud control arrangements, consistent with the Commonwealth Fraud Control Guidelines.
- 4.7 The audit addressed the following key elements of fraud control:
- fraud control arrangements integrated within ATO's corporate governance framework;
    - ⇒ all GST business areas included in the ATO Compliance sub-plan;
    - ⇒ fraud prevention and detection focussed on GST General Compliance only (the highest risk area);
    - ⇒ detection strategies and management of fraud investigations were assessed;
  - strategies, systems and processes used to prevent and detect GST fraud;
  - management of GST fraud investigations;
  - reporting of GST fraud; and
  - key Risk Rating Engine (RRE) controls.

## Audit Findings

- 4.8 ATO has systems and processes in place to prevent, detect, investigate and report GST fraud. These activities are undertaken and implemented across

business lines. However, ANAO considers that these activities need to be better integrated and coordinated if they are to underpin an effective GST fraud control framework.

4.9 ATO is currently revising its GST fraud control plan. This will allow ATO to undertake a comprehensive assessment of all GST fraud risks. The plan should also integrate GST fraud prevention, detection and mitigation strategies across ATO. ANAO has identified a number of areas where improvements could be made. These include:

- articulating ATO's overall fraud control strategy to staff and how the Commonwealth's definition of fraud is to be interpreted and implemented;
- recognising that external fraud should be treated as a separate component of ATO's compliance continuum;
- reviewing data collection requirements and the integrity of data to be included in fraud reports; and
- enhancing the effectiveness of the RRE as a fraud detection tool.

4.10 ANAO made eight recommendations, all of which were agreed to by ATO. In summary, ANAO recommended that ATO:

- articulate how the Commonwealth's definition of fraud is to be interpreted across the ATO;
- undertake an agency-wide co-ordinated assessment of GST fraud risks;
- review and report on its data integrity and collection requirements;
- undertake on-going evaluation of RRE fraud tests and business rules;
- reference fraud case notes to maximise the potential of the Registration Information Matching System (RIMS);
- record fraud cases in the Fraud Investigation Reporting and Management (FIRM) System;
- supply investigation guidelines to officers preparing briefs for the DPP; and
- evaluate and analyse fraud outcomes and trends routinely, to support agency fraud control planning and development.

## The Committee's Review

- 4.11 On 13 October 2003 the Committee held a public hearing to review ATO's progress against the audit's recommendations. The public hearing was attended by:
- Australian Taxation Office; and
  - Australian National Audit Office
- 4.12 The Committee took evidence on the following issues:
- definition of fraud;
  - international comparison of Australia's fraud control systems;
  - serious non-compliance capability;
  - cash economy;
  - recording and reporting; and
  - Risk Rating Engine (RRE).

## Definition of fraud

- 4.13 The Committee expressed concern that the definition of fraud was "too loose" for the purposes of ATO assessment of the veracity of many taxpayer GST-related records. It noted that ATO appeared to be hampered in achieving effective containment and successful prosecution of suspected fraud due to definitional vagueness. ANAO recommended in its audit report, and ATO agreed to articulate how fraud would be interpreted and implemented across ATO.
- 4.14 In response to the Committee's questions, ATO conceded that the existing definition of fraud was "...an extremely wide definition. It basically covers just about anything that we come across in a tax environment".<sup>2</sup> From the definition and the DPP guidelines there is no formula that determines "all of these add up to fraud".<sup>3</sup> ATO said that it is pessimistic about "ever getting an absolutely clear definition".<sup>4</sup>

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2 Australian Taxation Office (ATO), *Transcript, 13 October 2003*, p. 3.

3 ATO, *Transcript, 13 October 2004*, p. 2.

4 ATO, *Transcript, 13 October 2004*, p. 2.

4.15 ATO emphasised that for fraud to occur, it has to be seen that there has been *intent* to defraud, or some deception<sup>5</sup>. This matter is quite problematic for ATO. If someone has claimed a deduction they are not entitled to, ATO does not know whether they did it with intent, or if it was an innocent error.<sup>6</sup> The process and cost implications of ATO's response options are variable.

The area where we have difficulty is the borderline of where you make the decision about what you deal with administratively and what you refer to prosecution.<sup>7</sup>

4.16 ATO advised that the two most prevalent types of fraud were:

- where a taxpayer improperly claims a GST credit, and;
- invoice veracity, where non-arms length parties have concocted a transaction value. For example, there is a potential for fraud if one party to a transaction uses the accruals basis of accounting and the other party uses the cash basis and there is a non-arms-length valuation.

4.17 ATO emphasised that even where it harboured suspicions about a taxpayer;

Fraud is a very difficult offence to prove<sup>8</sup>

4.18 In the GST context, where a taxpayer claims an input tax credit but does not hold a valid tax invoice, ATO normally regards this as a compliance issue. If a taxpayer manufactures false documents to support such claims, then this is a fraud.

4.19 Other factors for ATO to consider in deciding the course of action on compliance, include materiality and past compliance history.

4.20 ATO advised that, in the context of the difficulties it experiences in proving fraud, rather than rely on a strict definition of fraud, it preferred to rely on on-the-ground referral guidelines and a bridging statement, as well as judgement on when to use a range of administrative solutions, rather than prosecution. ATO advised that its guidelines were in the process of refinement and were expected to be in place by early 2004.<sup>9</sup>

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5 ATO, *Transcript, 13 October 2003*, p. 3.

6 ATO, *Transcript, 13 October 2003*, p. 4.

7 ATO, *Transcript, 13 October 2003*, p. 2.

8 ATO, *Transcript, 13 October 2003*, p. 7.

9 ATO, *Transcript, 13 October 2003*, p. 8.

### Committee comment

- 4.21 The Committee is adamant that prevention of fraud is at the core of the integrity of a good GST system.
- 4.22 Evidence presented to the Committee shows that the Commonwealth's vague definition of fraud appears to allow some GST fraud to slip ATO's net and it is dismayed that ATO is pessimistic about tightening the definition of fraud.
- 4.23 The Committee endorses the risk management approach adopted by ATO, including consideration of taxpayer evasion history, financial materiality and evidence gathering as inputs to its decision whether to prosecute suspected GST fraud or not. ATO's undertaking to articulate the existing definitions of fraud, intent to defraud and the many examples cited in the Commonwealth Fraud Control Guidelines is seen as a step in the right direction.
- 4.24 ATO appears, however, to be constrained by the provisions in existing legislation in successfully prosecuting some suspected GST fraud and, instead, is forced to deal administratively with certain suspected breaches of a borderline nature. A more rigorous prosecution policy should be available to ATO to contain the incidence of GST fraud. Existing legislation that may form the basis for prosecution of suspected GST fraud should be reviewed to see if it can be tightened to enhance the ease of proof of fraud. The Committee recommends accordingly.

### Recommendation 4

- 4.25 **The Attorney-General's Department, in liaison with the Australian Taxation Office and the Commonwealth Director of Public Prosecutions, draft amendments to legislation, for the Attorney-General's consideration, that enhance the ease of proof in the prosecution of suspected Goods and Services Tax fraud.**

### International comparison of Australia's fraud control systems

- 4.26 The Committee questioned ATO as to how well the overall Australian GST data collection management regime, accountability and transparency compared with overseas counterparts.



- 4.27 ATO assured the Committee that it had designed its GST compliance program by considering a number of overseas regimes, at the time. These included Singapore which had implemented the most modern technological system; the United Kingdom's system which exhibited maturity; the Canadian system which showed a demographic fit; and New Zealand's system which possessed a credible GST policy model. Organisation of Economic and Cultural Development (OECD) papers and European Union arrangements were also reviewed.<sup>10</sup>
- 4.28 ATO had also perused the GST models of Australia's major trading partners, specifically Japan and China, but found that the systems in those jurisdictions were not comparable to Australia's. Japan had a different type of Value Added Tax (VAT) and China's tax administration was not as developed as other overseas regimes. The Committee noted in passing that another of Australia's major trading partners, the USA, has no GST.
- 4.29 Based on its research, ATO concluded that its international benchmarking had been made more robust through reference to systems in a number of countries which it believed were comparable to the Australian context, particularly the OECD, rather than countries solely with strong trade links to Australia.<sup>11</sup>

### Committee comment

- 4.30 The Committee is satisfied that ATO's benchmarking with overseas regimes has been thorough.

## Serious non-compliance capability

- 4.31 ATO advised the Committee that it had up-graded its serious non-compliance capability since the ANAO audit. Under the new structure, introduced in July 2003, its three former non-compliance functions – investigation, serious non-compliance and excise compliance – had been merged into a corporatised compliance program. The intent was to capture the benefits of critical mass as well as to allow practices, tools, resourcing and management of the program to be monitored and controlled. ATO reminded the Committee that it could only use tax powers for civil purposes and that for fraud only criminal investigation procedures could be used, necessitating the separation of the two

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10 ATO, *Transcript, 13 October 2003*, p. 4.

11 ATO, *Transcript, 13 October 2003*, p. 5.

functions. Notwithstanding, ATO advised it was seeking to merge its capability “because we need to be able to choose between those different strategies and use the most appropriate one for the circumstances”.<sup>12</sup>

4.32 Although it is early days, ATO advised that it was confident that the new arrangements were superior to the system they replaced. Two areas - albeit non-GST - were already being investigated.

### Committee comment

4.33 The Committee is satisfied that ATO has undertaken the appropriate upgrade of its serious non-compliance capability, in line with ANAO recommendations.

### Cash economy

4.34 Of concern to the Committee was the level of GST revenue lost through the operations of the cash economy, and questions were directed to ATO as to the methods used by ATO to estimate the magnitude of the cash economy.

4.35 ATO advised that:

there is not any agreed methodology to estimate the size of that cash economy.<sup>13</sup>

4.36 ATO indicated that it monitored academic, international and Australian Bureau of Statistics (ABS) research, but was unable to offer a firmer estimate of the magnitude of non-declared income other than equivalent to costing “billions of dollars of tax revenue” (including income taxes of sole traders and company taxes).

4.37 ATO’s administrative approach to making in-roads into non-declared income used:

- Australian Business Number (ABN);
- requirement for businesses to withhold at the top marginal tax rate for businesses not quoting an ABN;
- monitoring audit trails between parties using GST; and

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12 ATO, *Transcript, 13 October 2003*, p. 10.

13 ATO, *Transcript, 13 October 2003*, p. 6.

- verifying business records and business transactions with suppliers and customers.
- 4.38 ATO advised that, using the above methods, it was successful in bringing to account revenue that otherwise would be missing.
- 4.39 The Committee was advised by ATO that the introduction of the ABN system had resulted in the collection “at this stage, ... around \$60 million in back taxes from those businesses”<sup>14</sup> that had never been in the system. A far greater number of businesses were found by ATO than had been expected.

### Committee comment

- 4.40 The Committee, whilst appreciating that the size of the cash economy probably runs to billions of dollars and that the task of estimating the extent of the cash economy is enormous, recognises that not all tax revenue evaded results from GST fraud. It therefore concurs that ATO resources are better spent identifying non-declared income using the administrative tools mentioned above, and seeking appropriate penalties.
- 4.41 The Committee urges ATO to encourage ABS to intensify its research into methodologies to determine the extent of non-declared income in Australia.

### Recording and reporting

- 4.42 ANAO identified problems in recording and reporting by ATO with respect to the incidence of GST fraud and subsequent ATO action. Records on data bases were permitted to fall out of date as investigations proceeded.
- 4.43 The Committee asked ATO whether reporting and recording had been improved since the audit. ATO advised that a new case management system was scheduled for introduction in January 2004.<sup>15</sup> This system will envelope all areas that deal with fraud. Statistics will be collected and reports produced based on definitions devised in consultation with AGD. Manual monitoring will continue and will run in parallel with the new system until it is operating satisfactorily.

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14 ATO, *Transcript, 13 October 2003*, p. 16.

15 ATO, *Submission No. 5*, p. 2.

- 4.44 ATO advised that the reports produced will detail cases actually being investigated at the time.
- 4.45 In the case of interceptions of fraudulent or incorrect refunds, overseas experience and ATO's own risk assessments indicate that the most effective response by ATO is to intercept fraud prior to the refund being paid.
- 4.46 Compliance checks of businesses after GST refunds have actually been paid to tax payers, are carried out by a team of around 3 000 field officers which targets 10 per cent of the registered business population. These checks complement the interception activity noted above. Some 660 ATO field officers target the cash economy, of which 180 officers are specifically dedicated to the high risk building and construction industry. Techniques used include assessments of businesses for over-statement of expenses, visits to construction sites, checks to ensure sub-contractors are properly registered for GST and that they have reasonable arrangements in place to collect GST.
- 4.47 ATO advised the Committee that several entities had been prosecuted successfully, involving sums in the range \$6 million to \$13 million.
- 4.48 GST fraud investigations are generally selected on the basis of the significance of the suspected breaches, which was "not at the consumer end".<sup>16</sup> ATO confirmed, however, that it used other mechanisms to follow up GST evasion at "the lower end", including an evasion hot line.

### **Committee comment**

- 4.49 The Committee endorses ATO's attempts to identify and contain potential incidents of GST fraud before it happens.
- 4.50 The Committee is, however, concerned that ATO appears not to be able to quantify the tax gap – the difference between what is believed to be owed and what is actually collected.<sup>17</sup>
- 4.51 ATO's responses when questioned on their methods of measuring the extent of GST fraud appear to be indirect and vague, amounting to estimation by extrapolation. The Committee's view is that the basis of ATO's best estimate – "well over 80 percent,... close to 90 percent"<sup>18</sup> of the detection of fraud-based revenue before it is actually lost - is not sufficiently rigorous to stand as a credible performance measure. The

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16 ATO, *Transcript, 13 October 2003*, p. 14.

17 ANAO, *Audit Report No. 55, Goods and Services Tax Fraud Prevention and Control*, p. 51.

18 ATO, *Transcript, 13 October 2003*, p. 15.

Committee believes that ATO should establish and maintain a dynamic mechanism to determine an estimate of the tax gap using appropriate Australian Bureau of Statistics economy-wide business indicators.

- 4.52 Alternatively, the Committee believes that ATO's examination of a random sample of taxpayers to determine the level of compliance (and non-compliance) with GST obligations, which it performs as part of its performance agreement with the states and territories,<sup>19</sup> could be expanded to provide an estimate of the tax gap.
- 4.53 ATO should be able to report against a target performance measure of, say, 95 per cent collection of the theoretical maximum amount of GST owed, and the Committee recommends accordingly.

### Recommendation 5

- 4.54 **The Australian Taxation Office report to the Joint Committee of Public Accounts and Audit within six months, on a mechanism to estimate the tax gap, that would serve as the basis for reporting the overall efficacy of the range of measures being adopted to prevent and control Goods and Services Tax fraud.**

## Risk Rating Engine (RRE)

- 4.55 Given the crucial role that ATO's RRE plays in detecting fraudulent and non-compliant behaviour in the processing of activity statements, ANAO reviewed a number of the RRE's key controls. To put the importance of the RRE in context, ATO advised the Committee that a very robust pre-issue (of refunds) checking mechanism was necessary because of the huge number of forms handled annually by the GST system – 9.7 million Business Activity Statements and 2.4 million refunds.<sup>20</sup>
- 4.56 ATO advised the Committee that it has two automated checking mechanisms operating in tandem to detect compliance risk:
- Registration Information Matching System (RIMS) which checks registration consistency; and
  - RRE which checks activity statements automatically for consistency of current claims with the history of related business activity.

19 ANAO, Audit Report No. 55, *Goods and Services Tax Fraud Prevention and Control*, p. 50.

20 ATO, *Transcript*, 13 October 2003, p. 17.

- 4.57 File data are matched with current records and tests (some of which are dedicated fraud tests) are applied relating to various thresholds. If these checks show up high risk, the cases are immediately referred to the fraud intelligence area<sup>21</sup>.
- 4.58 The Committee questioned ATO whether there were any discernible trends relating to the level of fraud relating to those businesses using a tax agent to submit and those that did not. ATO advised that it had built in to its RRE the criterion of “not using a tax agent” as a higher risk. However it had found that there is not a discernible difference in what generates fraudulent compliance issues, whether a tax agent was used or not.

### **Committee comment**

- 4.59 The Committee is satisfied that the dual systems – RIMS and RRE- that ATO has in place for risk assessment of activity statements and tax payer profiles, are sufficiently robust to screen out high risk GST respondents. The automated systems are coping adequately with the huge volume of GST-related records processed annually.

Bob Charles MP  
Chairman  
March 2004

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21 ATO, *Transcript, 13 October 2003*, p. 18.



## **Appendix A — Conduct of the Committee's Review**

### **Selection of Audit Reports**

The Committee considered seven audit reports tabled late in the third quarter of 2002-03 and twenty seven audit reports tabled in the fourth quarter of 2002-03. These were:

- No. 30 Performance Audit  
*Defence Ordnance Safety and Suitability for Service*  
Department of Defence
- No. 31 Performance Audit  
*Retention of Military Personnel Follow-up Audit*  
Department of Defence
- No. 32 Business Support Process Audit  
*The Senate Order for Departmental and Agency Contracts (Spring 2002 Compliance)*  
Across Agency
- No. 33 Performance Audit  
*Management of e-Business in the Department of Education, Science and Training*  
Department of Education, Science and Training
- No. 34 Performance Audit  
*Pest and Disease Emergency Management Follow-up Report*  
Department of Agriculture, Fisheries and Forestry - Australia
- No. 35 Performance Audit  
*Fraud Control Arrangements in the Australian Customs Service*  
Australian Customs Service

- No. 36 Performance Audit  
*Monitoring of Industry Development Commitments under the IT Outsourcing Initiative*  
Department of Communications, Information Technology and the Arts
- No. 37 Performance Audit  
*Passport Services*  
Department of Foreign Affairs and Trade
- No. 38 Performance Audit  
*Referrals, Assessments and Approvals under the Environment Protection and Biodiversity Conservation Act 1999*  
Environment Australia
- No. 39 Performance Audit  
*Navy Operational Readiness*  
Department of Defence
- No. 40 Performance Audit  
*R&D Tax Concession*  
Department of Industry, Tourism and Resources, the Industry Research and Development Board and the Australian Taxation Office
- No. 41 Performance Audit  
*Annual Reporting on Ecologically Sustainable Development Across Agency*
- No. 42 Performance Audit  
*Managing Residential Aged Care Accreditation*  
The Aged Care Standards and Accreditation Agency Ltd
- No. 43 Performance Audit  
*The Sale of Sydney (Kingsford Smith) Airport*  
Across Agency
- No. 44 Performance Audit  
*Review of the Parenting Payment Single Program*  
Department of Family and Community Services
- No. 45 Business Support Process Audit  
*Reporting of Financial Statements and Audit Reports in Annual Reports*  
Across Agency
- No. 46 Performance Audit  
*Australian Industry Involvement Program*  
Department of Defence



- No. 47 Performance Audit  
*Implementation and Management of the Indigenous Employment Policy*  
Department of Employment and Workplace Relations
- No. 48 Performance Audit  
*Indigenous Land Corporation – Operations and Performance Follow-up Audit*  
Department of Immigration and Multicultural Affairs
- No. 49 Performance Audit  
*Management of the Navigation Aids Network*  
Australian Maritime Safety Authority
- No. 50 Information Support Services Audit  
*Managing People for Business Outcomes, Year Two*  
Across Agency
- No. 51 Performance Audit  
*Defence Housing and Relocation Services*  
Department of Defence
- No. 52 Performance Audit  
*Absence Management in the APS*  
Across Agency
- No. 53 Business Support Process Audit  
*Business Continuity Management Better Practices*  
Across Agency
- No. 54 Business Support Process Audit  
*Software Capitalisation*  
Across Agency
- No. 55 Performance Audit  
*Goods and Services Tax Fraud Prevention and Control*  
Australian Taxation Office
- No. 56 Performance Audit  
*Management of Specialist Information System Skills*  
Department of Defence
- No. 57 Performance Audit  
*Administration of the Payment of Tax by Non-Residents*  
Australian Taxation Office
- No. 58 Performance Audit  
*Veterans' Appeals Against Disability Compensation Decisions Follow-up Audit*  
Department of Veterans' Affairs, Veterans' Review Board

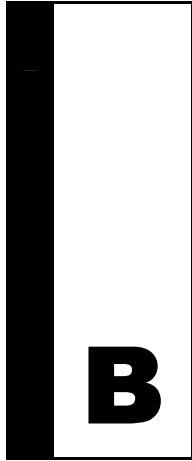
- No. 59 Performance Audit  
*Administration of Australian Business Number Registrations*  
Australian Taxation Office
- No. 60 Business Support Process Audit  
*Closing the Books*  
Across Agency
- No. 61 Financial Statement Audit  
*Control Structures as part of the Audit of Financial Statements of Major Commonwealth Entities for the Year Ending 30 June 2003*  
Across Agency
- No. 62 Performance Audit  
*Management of Selected Aspects of the Family Migration Program*  
Department of Immigration and Multicultural and Indigenous Affairs
- No. 63 Performance Audit  
*Administration of the Automotive Competitiveness and Investment Scheme*  
Department of Industry Tourism and Resources, Australian Customs Service

The Joint Committee of Public Accounts and Audit discussed the above audit reports and considered whether the issues and findings in the reports warranted further examination at a public hearing. In making this assessment the Committee considered, in relation to each audit report:

- the significance of the program or issues canvassed in the audit report;
- the significance of the audit findings;
- the response of the audited agencies, as detailed in each audit report; and
- the extent of any public interest in the audit report.

Following this consideration, the Committee decided to take evidence at public hearings on the following audit reports:

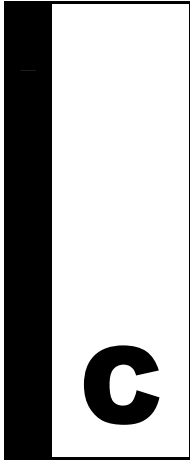
- No. 42 Performance Audit  
*Managing Residential Aged Care Accreditation*  
The Aged Care Standards and Accreditation Agency Ltd
- No. 51 Performance Audit  
*Defence Housing and Relocation Services*  
Department of Defence
- No. 55 Performance Audit  
*Goods and Services Tax Fraud Prevention and Control*  
Australian Taxation Office



## **Appendix B — Submissions**

1. Aged and Community Services Australia
2. Australian Nursing Homes & Extended Care Association Ltd
3. Defence Housing Authority
4. Australasian Auditing and Certification Services Pty Ltd
5. Australian Taxation Office
6. Defence Housing Authority
7. Australian Taxation Office
8. Australian Taxation Office





## **Appendix C — Exhibits**

1. Australian Taxation Office, *Compliance Program 2003-04*
2. Defence Housing Authority, *Review of Commonwealth Ownership of the Defence Housing Authority*





## **Appendix D — Witnesses Appearing at Public Hearings**

**Monday, 18 August 2003**

**Aged and Community Services Australia**

Mr Gregory Philip Mundy, Chief Executive Officer

Mrs Patricia Lee Sparrow, Policy Manager

**Aged Care Standards and Accreditation Agency Ltd**

Mr Mark William Brandon, Chief Executive Officer

Mr Ross John Bushrod, General Manager, Accreditation

**Australian National Audit Office**

Ms Deborah Jackson, Senior Director, Performance Audit Services Group

Mr John Emil Meert, Group Executive Director, Performance Audit Services Group

Dr Paul Nicoll, Executive Director, Performance Audit Services Group

**Australian Nursing Homes and Extended Care Association**

Mr Rod Young, Chief Executive Officer

**Catholic Health Australia**

Mr Richard Nelson Worsley Gray, Director Aged Care Services

**Department of Health and Ageing**

Ms Jane Olivia Bailey, Assistant Secretary, Quality Outcomes Branch

Mr Nick Mersiades, First Assistant Secretary, Ageing and Aged Care Division

**Monday, 15 September 2003****Australian National Audit Office**

Mr Warren John Cochrane, Group Executive Director, Performance Audit Services Group

Ms Danielle Smith, Performance Analyst, Performance Audit Services Group

Ms Nicola Thatcher, Director, Performance Audit Services Group

**Defence Housing Authority**

Mr Jon Howard Maxwell Brocklehurst, Chief Finance Officer

Mr Keith Thomas Lyon, Managing Director

**Department of Defence**

Mr Alan Henderson, Deputy Secretary, Corporate Services

Mr Ken Moore, Head, National Operations Division

**Monday, 13 October 2003****Australian National Audit Office**

Mrs Barbara Cass, Senior Director, Performance Audit Services Group

Mr Warren John Cochrane, Group Executive Director, Performance Audit Services Group

Mr Andrew Huey, Director, Performance Audit Services Group

**Australian Taxation Office**

Mr Christopher John Barlow, Assistant Commissioner, Serious Non-Compliance

Ms Jennifer Anne Granger, Second Commissioner

Mr John Neville Higham, Senior Assistant Deputy Commissioner, Goods and Services Tax General Compliance

Mr Neil Edward Mann, Deputy Commissioner, Small Business

Mr Barrie Thomas Russell, Deputy Commissioner, Goods and Services Tax