



HIGH COURT OF AUSTRALIA
Chief Executive and Principal Registrar

Parkes Place
CANBERRA ACT 2600

4 July 2008

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

Dear Mr Chafer

Thank you for the Committee's invitation to the High Court of Australia to make a submission to the *Inquiry into the Effect of the Efficiency Dividend on Small Agencies*.

The Court wishes to make the attached submission.

I would be available to discuss any issues raised by the Committee.

Yours sincerely

Andrew Phelan
Chief Executive & Principal Registrar

Submission by the High Court of Australia to the Inquiry by the Joint Committee of Public Accounts and Audit into the Effect of the Efficiency Dividend on Small Agencies

This submission provides an overview of the unique administrative characteristics of the High Court of Australia (HCA), outlines the effects of the efficiency dividend on the Court's administration and provides a short summary response to each of the Inquiry's Terms of Reference.

Overview of HCA Administration

The HCA was established by Section 71 of *The Constitution*. Statutory provisions covering the administration of the High Court appear primarily in Part III of the *High Court of Australia Act 1979* (HCA Act). Of particular relevance are s17 (Administration of the Court), s19 (Functions and powers of the Chief Executive and Principal Registrar – CE&PR) and s26 (Officers and employees). Part V deals with Court finances and accounts.

As a self-managing agency, separate from the Executive and Parliamentary branches of Australian governance, the HCA:

- allocates and manages its expenditure of appropriated and other moneys, for the purposes of the Court;
- employs its own staff; and
- is responsible for a range of assets, including the High Court Building in Canberra and a large law library (the Court also owns heritage books and artworks).

Relationship with Parliament and the Executive regarding Appropriations and Commonwealth financial processes

The Court may spend moneys appropriated to it by Parliament (s35 HCA Act) or other moneys (s39). Timings of the Court's draw-downs of its appropriated moneys are subject to directions from the Minister for Finance and Deregulation (the Finance Minister) but the Court is otherwise not subject to the financial controls exercised by the Finance Minister over other Commonwealth agencies. For example, unlike the other federal courts and other agencies in the Attorney-General's Portfolio, the HCA is not covered by the *Financial Management and Accountability Act 1997*. However, the Executive controls appropriations (s56 of the *Constitution*), so that the HCA is subject to the processes determined by Government for setting the amounts of moneys to be appropriated, inclusive of the rules set by the Finance Minister for costing agency outputs and any proposed new initiatives. The Court therefore participates in the Annual and Additional Estimates processes.

The current level of annual appropriations for the HCA owes more to history than any assessment of current need. It comprises a build-up of previous decisions by governments, overlaid by discounted, formulaic increases for

cost increases and the effects of the efficiency dividend. As with other Commonwealth agencies, apart from the wage cost indices (see below) there is no specific funding to meet actual increases in employee remuneration or other cost increases.

The Court is a “material agency” under the processes set by the Finance Minister, albeit solely because of the size of its net assets (inflated due to the value of the High Court Building in Canberra on the Court’s balance sheet).

The Court may not expend its appropriated moneys otherwise than in accordance with estimates approved by the Attorney-General (s36(2)). The Attorney-General should set the framework for seeking this approval (s36(1)).

The HCA collects filing and related fees (around \$1 million per annum), the rates of which are determined under the *High Court of Australia (Fees) Regulations 2004*. Fees received are treated as administered revenues and passed to consolidated revenue, although the legal basis for this is uncertain. The Court derives and retains income from renting legal practitioner rooms in the High Court Building in Canberra during hearings and some car parking spaces and by charging for some administrative services, but overall the amounts of non-appropriation revenues are minimal. The Court can retain and spend interest earned on its bank accounts.

The Court controls the expenditure of the appropriated and other moneys it receives (ss17, 37 and 39 HCA Act). However, some Ministerial (Attorney-General) responsibility is maintained through the estimates approval requirements referred to above and limitations placed on the Court’s ability to enter into contracts exceeding \$1 million in amount (s40 HCA Act and r4 HCA Regulations 2000) without approval by the Attorney-General.

The Court (through the CE&PR as employer) employs its own staff and determines their terms and conditions of employment (s26 HCA Act). Unlike in other Commonwealth courts and most other Commonwealth agencies, HCA employees are not covered by the *Public Service Act 1999*.

Effects of the efficiency dividend on the Court’s administration

Comprehensive reviews of HCA Registry and administrative processes have been conducted. PricewaterhouseCoopers has also reviewed the Court’s financial position and financial performance. These confirm that there is no scope to reduce costs without cutting significant elements of the Court’s operations. Moreover, the Court by its nature has very limited opportunities to secure additional funding through New Policy Proposals, but has attempted to do so where needs required it (eg, to cover the costs of repairing the roof of the Canberra Building).

When long term cost trends for salaries and unavoidable expenses, primarily relating to the High Court Building in Canberra and other accommodation, are overlaid with the recent increases to the efficiency dividend the Court is faced

with increasing deficits. The Court has written to the Attorney-General about this.

Major elements of HCA expenditure, especially for building, accommodation and communications costs, are either committed long term or unavoidable, and are predicted to increase at rates exceeding forward estimates of revenues. For example, 23% of the Court's annual expenditure is on depreciation for the High Court Building in Canberra and its contents, with around a further 10% representing rent and outgoings for Court accommodation, including for Melbourne and Adelaide. HCA rent payments are increased periodically according to market movements by the Department of Finance and Deregulation, the owner of the Melbourne and Adelaide buildings occupied by the Court, but appropriated revenues to fund the rent are not increased at the same rate and are in any case also reduced by the efficiency dividend. The widening gap between revenues and costs in these commitments imposes disproportionate pressures on other areas of the Court to reduce costs or to bear a higher rate of the efficiency dividend.

Employee salaries and related expenditure represent about half of total HCA annual expenditure. The Court currently has around 100 employees, many of whom (cleaners, attendants and court reporting staff) are casual or part time, resulting in a full time equivalent staffing number of around 85. The majority of staff are employed in the High Court Building in Canberra, with others located in Sydney, Melbourne and Brisbane.

As a small agency, with a relatively small number of employees spread nationally in four locations, the Court has minimum staffing requirements preventing further fractional reductions to meet the efficiency dividend. The Court is also materially affected by government policies limiting funding for increases in employee remuneration (as well as for increases in other actual supplier costs). The Court must attract and retain capable employees by providing competitive remuneration, but lacks the ability to find actual cost "productivities" or cost reductions elsewhere to fund increasing remuneration.

Agencies' appropriations are varied (increased) annually through the mechanism of wage cost indices (WCIs). There are several WCIs used for Commonwealth agencies, reflecting the mix of employee and non-employee costs for each agency. WCIs are based on changes to values of a basket of salary and related costs as they relate to "safety net amounts" for employee remuneration in a defined group of industries. It is neither a calculation of actual, average changes in employee remuneration generally nor an indicator of employee cost movements in the public sector. It is also not based on actual movements in supplier costs. However, WCIs are applied across both employee and non-employee costs in the Commonwealth, to produce basal increases in appropriations, before the application of the efficiency dividend to the result.

For several years the average national wage increase has been much higher than has been reflected in WCIs, even before the application of the efficiency

dividend. Similar disparities have prevailed between funding and actuality for supplier costs. The WCI is a poor surrogate measure of supplier cost increases, especially in “heated” areas like rent, other accommodation costs and ICT.

In this sense the discounted indexation for appropriations for employee and supplier costs has operated as a de facto efficiency dividend anyway, requiring increases to actual employee and supplier costs to be funded through cost reductions elsewhere. In the context of small agencies such as the HCA, where staffing is at minimum levels but requiring particular capabilities for which competitive salaries must be paid, and where supplier expenses are largely unavoidable in scope and increasing in cost through market forces, the levels of appropriation indexation operate as a further “efficiency dividend” additional to the actual efficiency dividend. Options for finding additional productivities to meet both the de facto and de jure efficiency dividends can be fewer for agencies with specialist employee requirements, as with the HCA (where as mentioned about half of the annual costs are employee-related). While options for contracting-out some services (including “piggy-backing” off contracts secured by larger agencies or groups of agencies to drive down prices) are exploited, options for the HCA have been few (largely for property maintenance, airline travel and office machine provision).

Salary and certain allowances for High Court Justices are paid by the Attorney-General’s Department from the standing appropriation in s7(13) of the *Remuneration Tribunal Act 1973*. Such funding is not subject to the efficiency dividend. However, other entitlements of High Court Justices (eg, staffing, vehicle entitlements, partner travel) are paid from the departmental item of the HCA’s annual appropriation, which is subject to the efficiency dividend. Remuneration of the CE&PR is also drawn initially from the standing appropriation under the Remuneration Tribunal Act, but unlike remuneration for Justices is re-appropriated in the HCA’s annual appropriation - at which point it becomes subject to the efficiency dividend. These inconsistencies are unreasonable per se; and there seems to be no justification for applying the efficiency dividend to these unavoidable costs. As the efficiency dividend is calculated on the whole of the annual departmental appropriations for the Court, the inability to reduce costs in these elements places disproportionate pressure on other elements. A point can be reached in a small agency like the HCA where there are no “discretionary” elements available to bear the costs of the efficiency dividend and core operations will therefore be adversely affected.

The decision to apply the “one-off” 2% increase in the efficiency dividend from 2007-08 and continuing through to 2011-12 inclusive was additional to the decision by the previous government to increase the dividend from 1% to 1.25% per annum from 2008-09.

The annual reductions in the Court's appropriations as a consequence of these two increases in the efficiency dividend (the "one-off" reductions are in brackets) are as follows:

2007-08	\$ 64,000 (\$64,000)
2008-09	317,000 (282,000)
2009-10	320,000 (284,000)
2010-11	322,000 (286,000)

As discussed above, the Court had predicted that it would move into deficits from 2008-09, before the application of the increased efficiency dividend. This trend towards deficits is because of the combined effects of salary increases for Court employees and supplier cost escalations, which are only partly covered by discounted annual increases in appropriations. In these circumstances, the application of the additional dividends could draw either of two possible responses by the Court – namely to operate at deficits further increased by the increases in the efficiency dividends or to cut essential parts of its operations. Given available cash reserves, it has sought approval for the former.

Summary response to each of the Inquiry's Terms of Reference

1. *Whether the efficiency dividend has a disproportionate impact on smaller agencies, including whether or not smaller agencies are disadvantaged by poorer economies of scale or a relative inability to obtain funding for new policy proposals.*

Under longstanding government policies, Commonwealth agencies are required to find continuing "productivities" to fund wage increases and efficiency dividends and sometimes to re-invest in infrastructure and new or improved processes. Over time, the capacity of agencies to find these productivities must, in general, reduce. The rate at which their capacity to do so will reflect both their starting positions (there was no level playing field at the time when the dividend commenced), their size (some economies come with scale, especially where agencies have the capacity to manage fractional reductions in salary costs) and ability to supplement their appropriations, either through charging for some services and retaining receipts (for example via agreements under s31 *Financial Management and Accountability Act 1997*), or through New Policy Proposals.

Efficiency dividends assume a level of inefficiency in all agencies equally and operate irrespective of the circumstances of each agency. In the case of the HCA, they are applied on the incorrect assumption that circumstances, measures and opportunities for efficiencies, which may or may not be applicable even in the Executive branch of Australian governance, also apply in the Judicial branch.

Smaller agencies tend to have less flexibility to absorb the impact of the efficiency dividend. This may, in part, be because they are generally

funded to achieve very specific outputs and outcomes, often with minimal allowance for support costs, dispersal of resources or extended lines of communications.

There are few if any workload funding models in operation, so appropriations are not adjusted for variations in workloads. Often small agencies become more productive (although this may not be sustainable, given work throughput stresses and limitations in infrastructures and other support resources) by managing increases in workloads with static or reducing levels of resources. In such cases, the efficiency dividend can be viewed as double-dipping the harvesting of productivities.

Smaller agencies have fewer opportunities to secure funding for new or changed programs through NPPs. Often any NPPs by smaller agencies are minor anyway, requiring savings offsets within portfolios which are unavailable or unable to be negotiated. In the case of the HCA, it is inappropriate that any increased funding for the Court be met by reducing funding for elements of another branch of Australian governance. Agencies which receive funding for NPPs are generally able to offset some, at least, of the impacts of the efficiency dividend in the way that administrative overheads are calculated. Efficiency dividend effects can be further moderated where multiple NPPs are agreed for an agency without discounting for scale effects. Sometimes, increases in departmental appropriations for such agencies may also be offset against savings in administered expenditures.

Larger agencies tend to have more ability to absorb "salami cuts". For example, if a function in an agency is performed by a team of 20 staff, by not filling one position a five percent reduction in costs may be achieved. In a smaller agency such as the HCA, particularly where there are minimum staffing requirements in different locations or particular skills requirements for particular functions, similar percentage reductions are more difficult or even impossible to achieve.

The longer term effect of the efficiency dividend for smaller agencies is the reduced capacity to sustainably support and deliver objectives. Over time, some agencies have dealt with efficiency dividends and other productivity demands (eg to fund salary increases) by cutting support services. While in part this may also reflect a lack of understanding of full, sustainable costs of delivering public sector functions and services, the consequences over time have been to reduce capability to sustain business processes and infrastructures.

- 2. Whether the efficiency dividend is now affecting the capacity of smaller agencies to perform core functions or to innovate.*

Reduced resources inclusive of reduced staffing levels, particularly in smaller agencies, even where they succeed in maintaining services, generally do not allow for any project capability to meet operating

challenges. It is possible in some agencies to operate a function with two or three staff, for example, but there may be no capability to improve services or perhaps even to implement infrastructure or process changes, hence over time reducing sustainability and eventually requiring specific funding injections.

3. *What measures small agencies are taking to implement the efficiency dividend, and the effect on their functions, performance and staffing arrangements.*

It is possible that smaller agencies are increasingly considering seeking approval to incur an operating loss, drawing on unspent cash appropriations relating to depreciation funding and the timing of capital acquisitions, to meet recurrent costs of the efficiency dividend. Clearly, such strategies are not sustainable.

Other strategies have included sharing resources where possible, although the most recent increases in the efficiency dividend have reduced the willingness or ability of many agencies to in effect subsidise other agencies through provision of free or discounted services.

4. *Any impacts of the efficiency dividend on the use by smaller agencies of "section 31" agreements to secure non-appropriation receipts (eg through user charges and cost recovery) - noting that these receipts are not subject to the efficiency dividend.*

The HCA is not covered by s31 of the *Financial Management and Accountability Act*, but has a provision (s39 HCA Act) which allows it to expend moneys received, other than through appropriations or which are held in trust, for the purposes of the Court. However, the Court has very limited opportunity to increase its receipts of "other moneys", for example through user charging and cost recovery; and to do so in core areas of the Court's operations (presumably requiring amendments to legislation covering fees) may also involve broader questions about access to justice and could not be undertaken unilaterally by the Court. Most other smaller agencies will have limited options to increase revenue from non-government sources. Where opportunities exist, they are unlikely to make a significant difference relative to the size of the efficiency dividend.

5. *How application of the efficiency dividend is affected by factors such as the nature of an agency's work (for example, cultural, scrutiny, or regulatory functions) or the degree of discretion in the functions performed by smaller agencies.*

See comments above about the unique administrative characteristics of the HCA. There are limits to the mechanisms which the Court can adopt to moderate the impact of the efficiency dividend, noting its separation from other branches of Australian governance and its role of interpreting The Constitution inclusive of actions of governments and legislatures.

6. *If appropriate, alternatives to an across-the-board efficiency dividend to encourage efficiency in the Commonwealth public sector, including consideration of whether certain agencies should be exempted from the efficiency dividend, or whether the rate of the dividend should vary according to agency size or function.*

Circumstances relevant to the Executive branch may not be relevant to the Judicial and Legislative branches and consideration might be given to understanding the differences when assessing whether the efficiency dividend should continue to apply to the non-Executive branches.

A number of agencies, inclusive of the HCA, probably require re-basing of their appropriations to address more-contemporary resource needs. Consideration might be given during re-basing as to whether the efficiency dividend should be applied in future or, if it should, whether a different rate might be applicable more appropriate to the characteristics of individual agencies.