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Opening Statement—JCPAA Inquiry into Efficiency Dividend
Public Service Commissioner
Friday, 19 September

The Australian Public Service Commission welcomes the inquiry and thanks the Committee for this opportunity to appear before it.

I have two roles in appearing today—first as Public Service Commissioner responsible for evaluating and reporting annually to Parliament on the state of the APS; and second, as the agency head and chief executive officer of a small agency. I will speak to both these roles today.

The efficiency dividend has been an important driver of efficiency improvement over many years in the Australian Public Service. Given current fiscal constraints, and the priority on curbing inflation, the APS needs to continue to be economically responsible. The key issue is how to ensure the APS operates in a sustainable way so that agencies of all sizes can deliver their core functions. Over time, it has become clear that small agencies in particular have found it more difficult to manage the ongoing application of the efficiency dividend.

As you would expect, the Commission's experience as a small agency is similar to that of other small agencies, although we also have unique challenges arising from the composition of our budget and the nature of our work.

We have fixed costs in relation to accommodation and a requirement to be represented in most states in Australia given that about two-thirds of public servants work outside Canberra. Over the past two years the Commission has been subjected to large market increases in rent owing to expiring leases and the need to fit out our new Canberra, Sydney and Perth offices. While our new leases represent best value for money, we have struggled to meet the increased rental costs and one-off movement expenses.

We are facing the challenge of meeting our obligations to staff under our workplace agreements and they are all up for renewal mid 2009. This imposes significant constraints on our staffing levels. Exploring new ways to increase the

Commission's earnings have been used to offset what would otherwise have been significant downsizing. There is a constant emphasis on seeking new revenue sources to enable further cost recovery to keep us afloat.

As part of the Group 8 cluster, our IT services provider contract comes to an end in June 2009 and cannot be extended. Group 8 is disbanding and we must now fund the costs of replacement services and managing the new arrangements independently. Unlike our larger Group 8 partners the Commission has not been able to afford progressive upgrades and our current infrastructure is outdated. The Commission's reliance on outdated technology has hindered our ability to use technology to drive efficiency improvements.

The indications are that we will be required to invest a much larger proportion of our budget into IT to bring our systems into line with the standards and IT capability applying in better resourced agencies. It is likely that this will involve substantial additional costs, even if we use the shared services of another agency or piggy-back on a different agency's contract. While it will deliver an IT generational change for the Commission, it will only be to today's levels, which leaves us with even more cost pressures as our ICT support needs increase.

The composition of the Commission's budget is unique in that we receive half of our funding through what is commonly known as 'section 31 receipts' on a cost-recovery basis for the delivery of services to other agencies—principally the delivery of learning and development programmes which is one of our core functions, but also employment services and gazette revenue. The amount of section 31 funding has been increasing steadily for us over the last 10 years from around thirty-five per cent of our base in 1997-98 to just below fifty per cent in 2007-08.

Around 80 people (or 40 per cent of the Commission's staff) will be funded off-budget in 2008-09 from revenue raising activities. The reliance on this revenue has limitations, and workplace planning is problematic.

Our budget outcome is at risk if we fail to meet revenue targets. If budgetary pressures on other agencies lead to a reduction in the demand for learning and development and other Commission employment services, this will lower the Commission's recovered revenue. This puts pressure on other areas of the Commission to reduce costs so the Commission's budget does not result in an operating loss, which in turn can compromise the delivery and timeliness of our statutory functions. While a loss in these circumstances may be manageable in any one financial year, it is not sustainable year-on-year.

Demand for the Commission's employment services is decreasing, particularly in regional Australia. Attendance at Commission learning and development programmes are also down on the forecast. It could well get to the point where I am forced to consider seriously the prospect of office closures or at least a major rationalisation.

The increased efficiency dividend, rising fixed costs, hard to predict swings in demand for our services and our unusual budgetary makeup makes budgetary management in the Commission particularly challenging.

The result is that we watch every dollar we spend and prioritise work corporately down to individual staff and projects. We have tackled underperformance and have a very minimal corporate team. We have been helped by other agencies who have given us staff at no cost to work on some projects. The Commission has made good use of limited resources and with the help of some new policy funding in recent years we have been able to produce some good results.

But we can't go on like this. Our core functions are being compromised, and there is much more that we should be doing and that agencies want us to do, to support them and individual public servants to fulfil their responsibilities.

I can't emphasise strongly enough that maintenance of the Commission's core functions, alongside those of the ANAO, is a sound investment in the quality, capability and integrity of the Australian Public Service. We cannot afford to let them be run down.

The Commission's fixed costs are 21% of total costs. Therefore, bearing in mind that nearly 50% of the Commission's budget is cost recovered from agencies, the actual application of the dividend from our appropriation in 2008-09 is 2.4% rather than 1.25%.

I have been concerned about the effects of the funding arrangements and the application of the efficiency dividend on small agencies for some years and have canvassed those issues in each of my State of the Service reports.

Last year's report demonstrates that the APS has shown high levels of productivity growth. The APS's results are better than productivity movements across the economy as a whole, which have been around 1.8 to 2% per annum. In the APS, efficiency dividend savings have been appropriated by governments since 1987–88, and have risen from 1 to 1.25% per annum in 2005–06 and to 3.25% in 2007-08. On top of this, APS agencies have also needed to find cost savings of around 1.75% a year, over and above budget supplementation to meet increases in employee wages. Even without including the new government measures that we have all absorbed, the cumulative effect of these APS measures has been an annual impact of at least 3% per year for the last decade and will be around 5% this year.

To give you a picture of how this plays out in practice, take the example of my own agency. In the last five years, the impact of the efficiency dividend has reduced the benefit of the indexation adjustment to our appropriation from the Government by 9%. The result in real terms is an indexation adjustment of only 2% over the same period. When cost increases in the order of 20% arising from our collective agreements and property lease costs are taken into account, there is an accumulative funding gap of 18% in just five years.

This year I included in the State of the Service report's agency survey some specific questions to investigate how the efficiency dividend is being managed across all agencies. By early November, when that data will have been checked and analysed, I will make the results available to the Committee.

Looking more generally at smaller agencies within the Australian Public Service, the ongoing application of the efficiency dividend is continuing to be difficult for small agencies to manage. The problem is compounded by the current indexation adjustment arrangements whereby indexation—less the efficiency dividend—does not keep pace with agencies' rising remuneration costs, which are generally around 4 per cent a year, leaving agencies to fund the difference from within their existing budgets. The cumulative effects of both the dividend and indexation policies are significant.

It may be timely for the consideration of a safety valve mechanism to be put in place, to protect small agencies and ensure their ongoing viability into the future in what will no doubt likely be a continuing challenging fiscal environment. In the development of such a 'safety valve', relevant considerations could include the quality of an agency's service management; its organisational capability; and its record in pursuing performance improvement.

As you have heard from the discussions conducted with agencies to date, the impact of the efficiency dividend differs from agency to agency. There are, however, some recurring issues and these include:

- agencies with high fixed costs are struggling to absorb the additional 2 per cent dividend—for example, the Family Court of Australia has 56 per cent of its budget allocated to fixed costs, leaving only 44 per cent of its budget to absorb the efficiency dividend; for the Federal Magistrates Court, the scenario is even worse, the Court has had to manage the efficiency dividend out of 15% of its budget appropriations
- managing staff carefully to fund the additional 2 per cent, and reducing investment in staff training and development activities to make short term budget gains;
- reducing conditions to make short term savings—for example, being accommodated in cheaper premises with limited staff amenities and careful scrutiny of all travel
- reducing core services to clients—for example, the collections institutions are reducing the number of travelling exhibitions interstate, particularly to regional and rural areas, or reducing services, such as the National Library

cutting advisors in its Reading Rooms and ceasing its Indonesian Collections Programme; the National Maritime Museum has cancelled exhibitions and the Ombudsman is referring clients back to originating agencies as it cannot absorb increasing volumes of requests; and

- reducing the quality of the core services delivered—for example, the ANAO reducing the number of audits it conducts, and the Insolvency and Trustee Service Australia reducing the extent to which it investigates alleged offences.

In much the same way, the Commission finds itself cancelling learning and development programmes due to insufficient numbers, investing less in programme enhancements which affects the quality of our training, providing fewer free support services to agencies and, if appropriate, using cost recovery for new services demanded by agencies. I worry that charging can be inappropriate and is undermining the public good aspect of the work we do, and I am certainly conscious that it is increasingly resented by agencies.

The impact of the efficiency dividend is reflected in staff working long hours in some agencies. I expect this is to pick up the slack when people leave, or when non-ongoing employees' contracts are not renewed. I hear many stories of increasing workloads and longer hours becoming the 'norm' in the workplace. Staff accept that vacant positions are not automatically filled – each position is being examined once it is vacated and on-going positions are not automatically advertised for permanent filling.

Small agencies are not able to offer salaries commensurate with those offered by larger agencies, and recruiting specialist staff in tight labour markets is becoming much more difficult. Remuneration is a challenge for many small agencies particularly where staff work long hours and are being paid at rates lower than others in their fields. Agencies offering higher remuneration are more attractive, particularly when the workloads are compared. Over time small agencies are likely to find it increasingly difficult to attract and retain quality staff in this environment. They may be at risk of investing significant resources into recruiting staff only to lose them shortly after they commence.

From an APS-wide perspective, there is a risk that the continued application of the efficiency dividend will result in quality staff with solid government and corporate knowledge leaving the service without transferring that knowledge to their colleagues. Reducing staff development and training opportunities will lower the capacity of existing staff to enhance existing skills, and develop new ones. Morale in small agencies may fall and result in quality staff moving to higher paying agencies, or leaving the public sector altogether to pursue a career in the private sector. Over a period of time, experienced staff will be fewer, which will impact on the public service's ability to provide good decision making to government.

On that note, I conclude my opening statement, and welcome questions from the Committee.