
The Parliament of the Commonwealth of Australia

Report 396

**Review of Auditor-General's Reports
2002-2003
First, Second & Third Quarters**

Joint Committee of Public Accounts and Audit

September 2003
Canberra

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ISBN [Click **here** and type ISBN Number]



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Foreword

Report 396 is the outcome of the review by the Joint Committee of Public Accounts and Audit of the Auditor-General's audit reports tabled in the first, second and third quarters of 2002–2003. Of the 29 audit reports reviewed, the Committee selected 11 for further examination at three public hearings.

Included in the 11 audit reports was a performance audit of the management by the Department of Transport and Regional Services of its responsibility to oversee aviation security in Australia. Following the Committee's examination of the audit report there were three serious aviation security incidents in Australia. The Committee subsequently extended its review under expanded terms of reference. The Committee will report the outcome of this review in a separate report.

The Committee's review of *Audit Report No. 2, 2002–2003, Grants Management ATSI*C has in part been overtaken by the establishment on 1 July 2003 of the Aboriginal and Torres Strait Islander Services agency (ATSIS). ATSIS now administers the Aboriginal and Torres Strait Islander Commission's (ATSI)C's grants program.

The management of the grants program faces a range of difficulties. These include the sheer number of organisations that receive funding, their geographical isolation, and the difficulty in attracting and retaining skilled staff to manage funded projects. The Committee was pleased that, at the time of the hearing, ATSI)C was exploring various options to address these difficulties.

Grants project officers are required to identify alternative sources of funding for applicants. The Australian National Audit Office (ANAO) found that the outcome of this strategy was heavily dependent on the knowledge of regional staff. The Committee considers that if ATSI)C Regional Councils could better access and distribute information about alternate source of funding, it would considerably lighten ATSI)C's funding load.

The Committee has recommended that ATSIIS investigate cost-effective methods of compiling and publishing information about alternative sources of funding from the three levels of government. The information should be provided to ATSIIC Regional Councils on a regular basis.

During its review of *Audit Report No. 3, 2002–2003, Facilities Management at HMAS Cereberus* the Committee was advised of serious deficiencies in the use of Defence's Audit Recommendations Management System (ARMS). Many of Defence's actions in response to the Committee's and ANAO's recommendations were being marked off by Defence personnel as 'complete' simply because the due date for action had been reached.

This potentially compromises the veracity of Defence's advice concerning its progress in implementing the recommendations to which it had agreed. The Committee has recommended that Defence immediately update ARMS and provide advice on the current status of all Committee and ANAO recommendations.

Audit Report No. 7, 2002–2003 was a follow up to a previous ANAO audit of client service in the Child Support Agency (CSA). The Committee had also reviewed this previous audit and made three recommendations when it reported to Parliament in 1999.

The ANAO audit, and subsequent evidence at the public hearing, revealed that the CSA had re-interpreted a Committee recommendation. The CSA had completed action in regard to the re-interpreted recommendation and reported to the Committee in an *Executive Minute* that the recommendation had been agreed to.

The Committee considers that its recommendations are sufficiently well-thought out and considered to warrant full implementation. If an agency disagrees with the recommendations of external reviewers it should make its concerns explicit to both its Minister and those reviewers. To do otherwise potentially misleads its Minister and (when parliamentary committee recommendations are involved) the Parliament.

The Committee has recommended that the CSA advise the Committee of progress towards implementing recommendations directed to it in the Committee's 1999 report.

The Committee reviewed CSA's debt management and acknowledges the ANAO's finding that debt management had improved. Debt management is an issue with broad financial and social implications. Child support debt means that CSA resources are required to pursue debt. As well, there is a potential impact on social security payments for carer benefits. The social impact of child support debt

means that children are not being adequately supported by their parents, which may have implications for the health, housing and education of these children.

The Committee has recommended that the CSA make a detailed report to the Committee on progress made in implementing new strategies to address debt management for its clients.

During its review of *Audit Report No. 18, 2002–2003, Management of Trust Monies* the Committee's attention was drawn to the management by Comcare of employee compensation payments. The ANAO noted that Comcare's treatment of such money, although less onerous, was not in accord with the correct treatment of special public monies. This issue has also been raised in a separate Committee inquiry. A submission to that inquiry by the Department of Finance and Administration indicated that amendments to the *Safety, Rehabilitation and Compensation Act 1998* would be included in the *Financial Framework Legislation Amendment Bill*.

Audit Report No. 19, 2002–2003 focused on the Australian Taxation Office's (ATO's) management of its relationship with tax agents. Tax agents form the core of the tax practitioner group and have a fundamental role in the effective operation of the tax system.

The Committee acknowledges the ATO's work on gathering information on the tax agent population. Currently such information concerns the demographics of tax agents, indicators of their business success, and factors which motivate and frustrate them. While the compliance profile of tax agents is part of future phases of the research, the Committee believes this important aspect of profiling should not be overlooked.

The Committee endorses the ATO's endeavour to improve its communication with tax agents through the introduction of the ATO internet tax agent portal. The Committee expects this system to be continually reviewed to take advantage of advances in information technology.

As part of its review of *Audit Report No. 25, 2002–2003, Financial Statements of Commonwealth Entities for 2001–02* the Committee revisited its recommendation in an earlier report that the Final Budget Outcome (FBO) be audited. The Committee notes the two significant impediments to achieving this goal: the need to determine which audit standards to use, and the difficulty in preparing and auditing the FBO within the three months specified by the *Charter of Budget Honesty*.

The Committee is encouraged by the move to harmonise Australian and international reporting standards, and the move to progressively bring forward the provision of financial information by agencies. While the Government has not agreed to the recommendation that the FBO be audited, the Committee still

believes in the merits of its recommendation. The Committee recognises, however, that the goal of the issuing of audited FBOs is achievable only in the medium term.

The financial statements of the ATO have been qualified by the ANAO for several years running. This was because the ATO's lease of its computer equipment had been recognised in the accounts as an operating lease, rather than as a finance lease in accordance with Australian accounting standards. The Committee notes that the leasing contract is due to expire and has recommended that the ATO review the terms of its leasing arrangements. The nature of the lease should be clarified so that the subsequent accounting treatment does not attract an audit qualification.

Audit Report No. 47, 1997–98, Management of Commonwealth Guarantees, Indemnities and Letters of Comfort drew attention to the parliamentary accountability procedures for the issuing of indemnities adopted by the United Kingdom Parliament. The Committee notes that the UK model provides the opportunity for the UK Parliament to become involved at an early stage in the creation of contingent liabilities. This contrasts with the system in Australia where contingent liabilities are reported after the event.

The Committee supports the earlier involvement of the Parliament in the creation of the Commonwealth's contingent liabilities. The Committee has recommended that the Commonwealth adopt procedures for notifying the Parliament of the issuing of indemnities based on the procedures used by the UK Parliament.

Audit Report No. 20, 2002–2003 reviewed the management of two employee entitlements support schemes by the Department for Employment and Workplace Relations (DEWR). The Committee notes that the administration of both the Employee Entitlements Support Scheme (EESS) and the General Employee Entitlements and Redundancy Scheme (GEERS) has been a major challenge for DEWR because these schemes were the first of their kind in Australia.

The Committee commends DEWR on its positive response to suggestions for improvement from both the ANAO and a consultant engaged by DEWR. The Committee notes that many of the suggestions and recommendations have already been partially or fully implemented.

The Committee recognises that insolvency practitioners have a substantial and essential role in the successful operation of EESS and GEERS. Consequently, DEWR's management of its relationship with insolvency practitioners will have a significant impact on the management of both EESS and GEERS. The Committee has recommended that DEWR examine ways in which it can monitor interactions between insolvency practitioners and individual claimants for the quality and accuracy of information provided to claimants.

As well, the Committee believes DEWR could take a more active role in promoting awareness of the schemes and has recommended that DEWR also examine ways in which it can improve claimants' awareness of the scheme, their eligibility for benefits under the scheme, and changes in the interpretation of the operational arrangements.

The Committee's review of *Audit Report No. 23, 2002–2003, Physical Security Arrangements in Commonwealth Agencies* revealed the different constraints faced by the sample of agencies called to the public hearing. Each agency must look for ways to address the security framework in the most effective and efficient way for the organisation involved. It is incumbent upon agencies, however, to ensure that training is relevant, accessible to all staff and maintains staff knowledge to current security standards.

The Committee notes that the agencies examined were aware of the importance of a thorough and timely response to security breaches and the importance of incorporating lessons gained from breaches into current security controls.

The final audit report examined in detail is *Audit Report No. 28, 2002–2003, Northern Territory Land Councils and the Aboriginals Benefit Account*. The Committee is pleased to note that all of the Land Councils subject to the audit have understood and acted upon the recommendations regarding risk assessment, management and accountability; and regarding the collection and use of performance information.

The Committee commends the Land Councils for having accepted the advice of the ANAO in a responsive and proactive manner and for having acted quickly to apply the advice to their organisational practices.

Bob Charles MP

Chairman



Membership of the Committee

40th Parliament

Chairman Mr Bob Charles MP

Deputy Chair Ms Tanya Plibersek MP

Members	Senator Richard Colbeck (until 25/03/03)	Mr Steven Ciobo MP
	Senator Stephen Conroy (until 10/09/03)	Mr John Cobb MP
	Senator John Hogg (from 10/09/03)	Mr Petro Georgiou MP
	Senator Gary Humphries (from 25/03/03)	Ms Sharon Grierson MP
	Senator Kate Lundy (from 19/11/02)	Mr Alan Griffin MP
	Senator Claire Moore (until 19/11/02)	Ms Catherine King MP
	Senator Andrew Murray	Mr Peter King MP
	Senator Nigel Scullion	The Hon Alex Somlyay MP
	Senator John Watson	

Membership of the Sectional Committee

40th Parliament

Chairman Mr Bob Charles MP

Deputy Chair Ms Tanya Plibersek MP

Members Senator Stephen Conroy
 Senator John Watson

Mr Steven Ciobo MP

Mr Petro Georgiou MP

Ms Sharon Grierson MP

Ms Catherine King MP

Committee Secretariat

A/g Secretary Mr James Catchpole

Inquiry staff Dr John Carter

Ms MaryEllen Miller

Ms Mary-Kate Jurcevic

Ms Maria Pappas

Ms Sheridan Johnson



List of abbreviations

AAS31	Australian Accounting Standing 31
ABA	Aboriginals Benefit Account
ABC	Australian Broadcasting Corporation
AFP	Australian Federal Police
AGS	Australian Government Solicitor
ALC	Anindilyakwa Land Council
ALRA	Aboriginal Land Rights Act
ANAO	Australian National Audit Office
ANSTO	Australian Nuclear Science & Technology Organisation
ARMS	Audit Recommendations Management System
ASC	Australian Submarine Corporation
ASIO	Australian Security Intelligence Organisation
ATO	Australian Tax Office
ATSIC	Aboriginal and Torres Strait Islander Commission
ATSIS	Aboriginal and Torres Strait Islander Services agency
BAS	Business Activity Statement

CAC	Commonwealth Authorities and Companies Act, 1997
CDEP	Community Development Employment Projects
CFS	Consolidated Financial Statements
CHIP	Community Housing and Infrastructure Program
CLC	Central Land Council
CMC	Comprehensive Maintenance Contract
COAG	Council of Australian Governments
CSA	Child Support Agency
Defence	Department of Defence
DEMS	Defence Estate Management Systems
DEO	Defence Estate Organisations
DEWR	Department of Employment and Workplace Relations
DoTARS	Department of Transport and Regional Services
EESS	Employee Entitlements Support Scheme
ETM	Economic Transactions Method
EWA	Employer Withholding of Arrears
HMAS	Her Majesty's Australian Ship
FBO	Final Budget Outcome
Finance	Department of Finance and Administration
FMA	Financial Management and Accountability Act
GEERS	General Employee Entitlements and Redundancy Scheme
GFS	Government Finance Statistics
GST	Goods & Services Tax
ID	Infrastructure Division

IGD	Inspector-General Division
IT	information technology
JCPAA	Joint Committee of Public Accounts and Audit
MOU	Memorandum of Understanding
NLC	Northern Land Council
OEC	Organisation for Economic Co-operation and Development
PM&C	Department of Prime Minister and Cabinet
PSCC	Protective Security Coordination Centre
PSM	Protective Security Manual
SDSS	Standard Defence Supply System
SEESA	Special Employee Entitlements and Redundancy Scheme for Ansett group employees
SFPALC	Senate Finance and Public Administration Legislation Committee
SRC	Safety, Rehabilitation and Compensation ACT, 1998
TABs	Tax Agent's Boards
TLC	Tiwi Land Council
TLM	Taxation Liability Method
TPG&A	Tax Practitioner and Alliances Branch
UMP/ AMIL	United Medical Protection Ltd/Australasian Medical Insurance Ltd

List of recommendations

Recommendation 1

- 2.39 The Aboriginal and Torres Strait Islander Services agency should investigate cost-effective methods of compiling and publishing information about alternative sources of funding from the three levels of government. This information should be provided to Aboriginal and Torres Strait Islander Commission Regional Councils on a regular basis.

Recommendation 2

- 3.33 The Department of Defence should immediately update its Audit Recommendations Management System and provide the Committee and the Australian National Audit Office with a report on the current status of all Committee and Audit Office recommendations.

Recommendation 3

- 4.32 The Child Support Agency should advise the Joint Committee of Public Accounts and Audit of the Agency's progress towards implementing the recommendations directed to it in *Report 367, Review of Auditor-General's Reports 1997-98, Third Quarter*.

Recommendation 4

4.67 The Committee recommends that the Child Support Agency make a detailed report to the Committee on progress made in implementing new strategies to address debt management for clients of the Child Support Agency.

Recommendation 5

7.66 The Australian Taxation Office should review the terms of its information technology outsourcing contract when the contract is renewed so that the nature of the lease is clarified and the subsequent accounting treatment does not attract an audit qualification.

Recommendation 6

8.39 The Commonwealth should adopt procedures for notifying the Parliament of the issuing of indemnities based on the procedures used by the United Kingdom Parliament.

Recommendation 7

9.62 The Department of Employment and Workplace Relations examine ways in which it can:

- improve claimants' awareness of the scheme, their eligibility for benefits under the scheme, and changes in the interpretation of the operational arrangements; and
- monitor interactions between insolvency practitioners and individual claimants for the quality and accuracy of information provided to claimants.

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 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 findings;
 - the arguments advanced by the audited agencies; and
 - the public interest of the report.
- 1.2 Upon consideration of 29 audit reports presented to the Parliament by the Auditor-General during the first, second, and third quarters of 2002–03, the Committee selected 11 reports for further scrutiny at public hearings. The public hearings were held in Canberra on:
- Friday, 28 March 2003;
 - Wednesday, 30 April 2003; and
 - Wednesday, 21 May 2003.
- 1.3 An inspection of the security arrangements at Sydney’s Kingsford Smith Airport was also held on Tuesday, 20 May 2003.

1.4 The 11 audit reports selected for the public hearings were:

Friday, 28 March 2003

- *Audit Report No. 2, 2002–2003, Grants Management ATSIIC (Chapter 2);*
- *Audit Report No. 3, 2002–2003, Facilities Management at HMAS Cerberus, Department of Defence (Chapter 3); and*
- *Audit Report No. 7, 2002–2003, Client Service in the Child Support Agency, Follow Up Audit, Child Support Agency (Chapter 4);*

Wednesday, 30 April 2003

- *Audit Report No. 18, 2002–2003, Business Support Process Audit, Management of Trust Monies (Chapter 5);*
- *Audit Report No. 19, 2002–2003, Performance Audit, The Australian Taxation Office's Management of its Relationship with Tax Practitioners, Australian Taxation Office; (Chapter 6);*
- *Audit Report No. 25, 2002–2003, Financial Statement Audit, Audits of the Financial Statements of Commonwealth Entities for the Period Ended 30 June 2002 (Chapter 7); and*
- *Audit Report No. 27, 2002–2003, Performance Audit, Management of Commonwealth Guarantees, Warranties, Indemnities and Letters of Comfort (Chapter 8);*

Wednesday, 21 May 2003

- *Audit Report No. 20, 2002–2003, Performance Audit, Employee Entitlements Support Schemes, Department of Employment and Workplace Relations (Chapter 9);*
- *Audit Report No. 23, 2002–2003, Protective Security Audit, Physical Security Arrangements in Commonwealth Agencies (Chapter 10);*
- *Audit Report No. 26, 2002–2003, Performance Audit, Aviation Security in Australia, Department of Transport and Regional Services; and*
- *Audit Report No. 28, 2002–2003, Performance Audit, Northern Territory Land Councils and the Aboriginal Benefit Account (Chapter 11).*

The Committee's report

- 1.5 This report of the Committee's examination draws attention to the main issues raised at the public hearings. Where appropriate, the Committee has commented on unresolved or contentious issues and made recommendations.
- 1.6 The report has the following appendices:
- Appendix A—a list of submissions received;
 - Appendix B—a list of exhibits received;
 - Appendix C—a list of the witnesses appearing at the public hearings; and
 - Appendix D—details of the inspection visit to Sydney's Kingsford Smith Airport.
- 1.7 A copy of this report is available on the Committee's website at <http://www.aph.gov.au/house/committee/jpaa/reports.htm>

Review of aviation security by the Committee

- 1.8 Following examination of *Audit Report No. 26, 2002–2003, Aviation Security in Australia* on 21 May 2003, there were three serious security incidents at Australian airports. These were:
- 22 May 2003—members of the public entered a secure area at Sydney Airport resulting in the shutdown of a domestic terminal;
 - 29 May 2003—the attempted hijack of an aircraft flying between Melbourne and Launceston; and
 - 30 May 2003—unscreened passengers entered a secure area at Sydney Airport resulting in the shutdown of a domestic terminal.
- 1.9 In light of these incidents and the heightened security environment existing in Australia, the Committee resolved on 4 June 2003 to extend the review of *Audit Report No. 26, 2002–2003*, under expanded terms of reference.
- 1.10 The terms of reference adopted by the Committee were:
- As part of its statutory responsibility to examine reports from the Auditor-General, the Joint Committee of Public Accounts and Audit is expanding its review of *Audit Report No. 26, 2002–2003*,

Aviation Security in Australia, Department of Transport and Regional Services to inquire and report on:

- regulation of aviation security by the Commonwealth Department of Transport and Regional Services;
- compliance with Commonwealth security requirements by airport operators at major and regional airports;
- compliance with Commonwealth security requirements by airlines;
- the impact of overseas security requirements on Australian aviation security;
- cost imposts of security upgrades, particularly for regional airports;
- privacy implications of greater security measures; and
- opportunities to enhance security measures presented by current and emerging technologies.

1.11 The Committee will report the outcome of this review separately.

Audit Report No. 2, 2002 - 2003

Grants Management ATSI

Introduction

Background

- 2.1 The Aboriginal and Torres Strait Islander Commission's (ATSI's) vision is to help Aboriginal and Torres Strait Islander peoples and communities exercise their legal, economic, social, cultural and political rights. The ATSI grants program provides financial assistance to individuals, communities and other levels of government as one means of achieving this vision.
- 2.2 ATSI is made up of an elected arm and an administrative arm. Elections are held every three years to fill positions on the 35 regional councils located throughout Australia. Each regional council makes its own funding decisions, based on a specific regional development plan that highlights the funding priorities for that region. The majority of ATSI grants are administered at a regional level.

- 2.3 In 2001–02, ATSIC provided grants of approximately \$869 million to indigenous organisations and State and Territory governments. This involved 3108 separate grants to over 1000 separate organisations to provide services to indigenous communities. Approximately 78 per cent of ATSIC grant funding is used to achieve objectives under two key ATSIC programs:
- Community Development Employment Projects (CDEP); and
 - the Community Housing and Infrastructure Program (CHIP).¹
- 2.4 On 1 July 2003, there was a significant change to the management of ATSIC’s grants with the establishment of the Aboriginal and Torres Strait Islander Services agency (ATSIS). The role of ATSIS is to ‘provide a range of policy, program and administrative services to ATSIC to assist it to achieve its national objectives.’ In short, ATSIS now administers ATSIC’s grants program.
- 2.5 The purpose of the change was to:
- ... provide better opportunities for ATSIC to focus on national policy development and advocacy; and for ATSIC Regional Councils to focus on regional-level planning and the coordination of services with the three levels of government, while seeking to improve the overall accountability for relevant program resources.²

The audit

- 2.6 The audit was conducted before the administrative changes introduced on 1 July 2003. It examined ATSIC’s grant management practices, as measured against recognised best practice standards set out in the ANAO Better Practice Guide published in May 2003.³
- 2.7 The audit concentrated on CDEP grants and regional council discretionary funding, representing approximately 84 per cent of all regional council grant funding. The audit did not cover in detail the administration of CHIP grants nor did it examine the appropriateness of funding decisions made by regional councils.⁴

¹ Auditor-General, *Audit Report No. 2, 2002–2003 Grants Management ATSIC*, Canberra, July 2002, p. 11.

² *Portfolio Budget Statements 2002–04, Immigration and Multicultural and Indigenous Affairs Portfolio, Budget Related Paper No. 1.12*, p. 173.

³ Auditor-General, *Administration of Grants*, Canberra, May 2002.

⁴ Auditor-General, *Audit Report No. 2, 2002–2003*, p. 12.

Audit findings

2.8 *Audit Report No. 2, 2002 – 2003, Grants Management ATSIC* found that:

- ATSIC had developed effective policies and procedures for administering grants that meet better practice standards;
- the financial management of grants , especially funds release and acquittals, was sound, however, the implementation of these policies and procedures lacked consistency among the regional offices;
- ATSIC, rather than providing supplementary funding, had assumed the role of a primary funder of programs and service to indigenous communities where mainstream programs were unable to cope with the needs of these communities;
- ATSIC grants were often historically based, thereby locking regional councils into a cyclical funding pattern;
- in assessing grant submissions, ATSIC had developed a risk management policy that was consistent with ANAO better practices and industry standards, however the discretion that regions were allowed had led to inconsistencies in how this policy was implemented;
- the decision-making by regional councils concerning grant approvals required further documented justification of reasons for full or partial funding of a submission, in order to make the process more transparent and to enable regional council decisions to stand up to greater scrutiny; and
- there was scope for improvement in ATSIC's management of approved grants, in particular with regard to the administrative requirements placed on small and struggling grantee organisations—many processes required improvement, for example clearer documentation and monitoring of grants through field visits.

The Committee's review

2.9 On 28 March 2003, the Committee held a public hearing to review the progress made by ATSIC in relation to the implementation of the ANAO's recommendations.

2.10 The Committee took evidence on the following issues:

- identifying funding priorities;
- managing approved grants;
- other options for managing grant funding; and

- alternative funding sources for indigenous communities.

Identifying funding priorities

- 2.11 One of ATSIC's roles is to fund programs for indigenous Australians that supplement funding from other government agencies. Identifying where gaps exist between the needs of indigenous Australians and the services provided by other government agencies highlights where supplementary funding is required.
- 2.12 The issue of apparent recurrent funding arose during the discussion about identifying the needs of communities. The audit report noted that ATSIC had not developed systematic methods to collect and document information to identify the needs of indigenous communities. One of the key findings of the audit was that the lack of information had caused many of the grants administered by ATSIC to become historically based and, as such, had committed the program to cyclical funding.⁵
- 2.13 This risked the perception that the funding was recurrent. The ANAO observed that:
- ... regions have a number of grantee organisations expecting the continuation of funding (and a portion of the council that believes they are entitled to it) that may not fit within the regional council priorities. As a result, potential grantee organisations that fit within a council's priorities cannot access these funds.⁶
- 2.14 The audit report identified the potential problems that may arise from cyclical funding:
- By continuing to fund incumbent grantees, ATSIC may create a perception that the submission process is a formality and that funding can be expected for the coming financial year. It also creates a significant barrier to any other indigenous organisations wishing to obtain a grant to address need within the region, as grant funds are limited ... Further, the cyclical and ongoing nature of the majority of ATSIC grant funding indicates that ATSIC is acting as a primary funder rather than a supplementary funder.⁷
- 2.15 As a consequence, the Auditor-General had recommended that:

⁵ Auditor-General, *Audit Report No. 2, 2002-2003*, pp. 31-2.

⁶ Auditor-General, *Audit Report No. 2, 2002-2003*, p. 31.

⁷ Auditor-General, *Audit Report No. 2, 2002-2003*, pp. 32-3.

ATSIIC develop a systematic method of collating information to identify funding needs within indigenous communities.⁸

- 2.16 ATSIIC agreed that the funding needed to be better targeted and noted that the board of ATSIIC had recently called for a review of the formula that underpinned their grants funding. ATSIIC told the Committee that this review would address one of the major concerns of the ANAO report:

Clearly, that priority is going to be in front of us to ensure better alignment between levels of grants, nature of grants and needs in different areas. So, in that sense we are picking up the thrust of the report: there is too much history driving what is happening, rather than a fresh assessment of relative need and relative levels of funding.⁹

- 2.17 ATSIIC added that it had, in response to the audit, established a unit to improve the collection and management of data on the needs of indigenous communities. This unit was planning some major survey work and was working cooperatively with the Bureau of Statistics and the Productivity Commission. The unit would also be working with the program of the Council of Australian Governments (COAG). ATSIIC anticipated that COAG's first report on Indigenous disadvantage would be an important tool to assist in its work.¹⁰

Committee comment

- 2.18 The Committee shares the ANAO's concern regarding supplementary funding versus recurrent funding and considers that ATSIIC needs to clarify the priority needs of communities to ensure that funding is best directed to areas of most need. The Committee endorses the Auditor-General's recommendation that ATSIIC develop a systematic method of collating information to identify funding needs within Indigenous communities and notes that ATSIIC has responded to this recommendation with the establishment of a unit that will address some of these matters.

Managing approved grants

- 2.19 The audit report concluded that while practice and procedures relating to the financial management of grants were appropriate and sound, there

⁸ Auditor-General, *Audit Report No. 2, 2002–2003*, p. 18.

⁹ Mr Bernard Yates, *Transcript*, 28 March 2003, p. 4.

¹⁰ Mr Bernard Yates, *Transcript*, 28 March 2003, p. 7.

was scope for improvement in ATSIIC's ongoing administrative management of approved grants.

2.20 The report observed that ATSIIC now needed to focus on the management of non-financial aspects of the process, such as adequate documentation and undertaking the required number of field visits to monitor grants, while still ensuring that gains made in financial management were not lost.¹¹

2.21 During questioning, ATSIIC agreed that there were problems in the management of grants and in achieving the outcomes set out by the grant proposals. ATSIIC commented that:

How to manage those funds and get the outcomes you are trying to achieve from those funds is the difficulty. A lot of these organisations have been operating for two or three years. They have not been operating in this environment with a background of [many] years. It is something we are cognisant of and are doing something about.¹²

2.22 ATSIIC detailed some of the issues affecting grants management, highlighting:

- issues of isolation which impacted upon education and skill levels in remote communities;
- limited capacity to attract skilled staff;
- lack of experience by organisations awarded grants; and
- the large number of communities that are able to seek funding from ATSIIC.¹³

2.23 The Committee questioned ATSIIC about the resources used to support organisations managing grants. ATSIIC confirmed there were options available for assisting organisations that were struggling with the administration of grants, such as the installation of grant controllers. However, ATSIIC agreed that more needed to be done, and commented on the difficulty of providing assistance while respecting the autonomy of each organisation:

We take action when organisations have more difficulty than we can allow, but we have to be cognisant of the control element as

¹¹ Auditor-General, *Audit Report No. 2, 2002–2003*, pp. 60–1.

¹² Mr Stephen Mason, *Transcript*, 28 March 2003, p. 8.

¹³ Mr Stephen Mason, *Transcript*, 28 March 2003, p. 8.

against the development element and the understanding of self-management. We cannot be controlling all organisations.¹⁴

2.24 The audit report highlighted the inconsistencies in various regions regarding the use of field visits as a monitoring tool. ATSIK's submission noted that it had asked Regional Managers 'to give field visits a high priority' as part of the monitoring that was integral to managing grants.¹⁵

2.25 ATSIK told the Committee that it agreed with the ANAO view that more needed to be done to support organisations that had received funding. Its comments reflected the understanding that grants management had been a problematic area for ATSIK and that, without further review, the problems would continue:

We need to develop, contract in or buy expertise in the area of community development ... and capacity building. A lot of our communities, of course, have suffered a mismatch between traditional governance and modern governance...So there are a number of issues we have to deal with ... Is there more to be done? Absolutely.¹⁶

Other options for managing grant funding

2.26 ATSIK took the opportunity at the hearing to outline some of the new initiatives for managing grant funding that it had trialled. An example was the use of contract program managers for some of the large housing infrastructure projects. ATSIK explained:

A lot of those [projects] are done through the use of contract program managers, where the community does not get the money but, rather it goes to a large international engineering firm. They negotiate with the community on the outcomes and the employment, and all the other spin-offs from the capital construction. They manage the contracting and the actual capital construction on behalf of the community. That is an instance where the community is still the nominal grantee. It owns the project but all the management and financial accountability goes through a contracted program manager.¹⁷

2.27 In other examples, ATSIK described how the allocation of grant monies was being managed in conjunction with State and Federal agencies:

¹⁴ Mr Stephen Mason, *Transcript*, 28 March 2003, p. 9.

¹⁵ ATSIK, *Submission No 1*, p. 6.

¹⁶ Mr Stephen Mason, *Transcript*, 28 March 2003, p. 10.

¹⁷ Mr Terrence Mowle, *Transcript*, 28 March 2003, p. 10.

In New South Wales we provide a grant of \$12.5 million to the Aboriginal Housing Office. Family and Community Services put in their Commonwealth-State Housing Agreement for that agency. That agency delivers one program of \$70 – odd million, provides one operational plan to ATSIC and FaCS and accounts for everything in through that one report.¹⁸

- 2.28 ATSIC advised that it was examining its submission process and methods of more effectively delivering grant funds. Over the next 12 months it would review aspects of contracted services, different service providers and purchaser-provider models. ATSIC noted that this would be ‘an extensive examination.’¹⁹

Committee comment

- 2.29 The Committee recognises the range of difficulties facing ATSIC in regard to the management of approved grants. These include the sheer number of organisations that receive funding from ATSIC. As well, there are issues of isolation and difficulty in attracting and retaining skilled staff to manage funded projects. The Committee is pleased that, at the time of the hearing, ATSIC was exploring various options such as contracted service delivery and entering into funding partnerships with State and Federal agencies. The Committee endorses the view of the ANAO that while ATSIC had made much progress in developing appropriate procedures and polices, the next challenge lies in ensuring the consistent application of these polices across all of ATSIC’s regional councils.

Alternative funding sources

- 2.30 ATSIC’s *Grants Procedures* manual requires project officers to identify alternative sources of funding for applicants. The ANAO found that in practice this relied heavily on the regional staff’s knowledge of what was available from all levels of government in their region. The ANAO noted, however, that the extent of this knowledge varied significantly from region to region. Some regions had developed information resources on the different funders available in that region for the information of staff and applicants.²⁰

¹⁸ Mr Terrence Mowle, *Transcript*, 28 March 2003, p. 5.

¹⁹ Mr Stephen Mason, *Transcript*, 28 March 2003, p. 5.

²⁰ Auditor-General, *Audit Report No. 2, 2002–2003*, p. 30.

2.31 The audit report also referred to the importance of advocacy on the part of ATSIC to develop awareness in the communities of alternative sources of funding to relieve the pressure on the availability of ATSIC grant monies.²¹

2.32 ATSIC agreed that knowledge about alternative sources of funding for Indigenous organisations was an important issue. However, ATSIC noted that unfortunately it was often the first point of call for organisations seeking funding when in fact many other options for funding were more appropriate. ATSIC commented:

Our presence and our funding are often the only resources that people feel that they have to work with.²²

2.33 The Committee enquired about what steps had been taken by ATSIC to enhance the information used to make decisions about funding priorities and alternative sources of funding.²³

2.34 ATSIC responded that the 35 regional councils were required to develop regional plans which included references to resource options for that community. ATSIC conceded, however, that it did not 'play a particularly active broker role in that regard.'²⁴

2.35 ATSIC also conceded that the highly complex environment of government services at various levels resulted in many organisations being unaware of the services and funding available to them.²⁵

2.36 While ATSIC stated that although there was a need and a demonstrated capacity for ATSIC to direct communities to other funding sources or to broker alternative funding arrangements with other government agencies, a considerable depth of knowledge and resources was required:

The difficulty is that we have a number of programs. Each department has a number of programs with a number of guidelines, a number of stipulations. For ATSIC as a whole to know the intricacies of all of those, I think that would require quite a large increase in resources ...²⁶

²¹ Auditor-General, *Audit Report No. 2, 2002–2003*, p. 34.

²² Mr Bernard Yates, *Transcript*, 28 March 2003, p. 6.

²³ *Transcript*, 28 March 2003, p. 11.

²⁴ Mr Bernard Yates, *Transcript*, 28 March 2003, p. 11.

²⁵ Mr Bernard Yates, *Transcript*, 28 March 2003, p. 11.

²⁶ Mr Stephen Mason, *Transcript*, 28 March 2003, p. 12.

Committee comment

- 2.37 The Committee agrees that it is a very large and complex task for any one agency to be fully aware of and provide advice on alternative sources of funding, within all three levels of government. However, it is the view of the Committee that if ATSIC Regional Councils could better access and distribute this information, it would lighten ATSIC's funding load considerably by directing organisations and communities to alternate source of funding.
- 2.38 An effective way to provide up-to-date information could be via ATSI's website. Using such a vehicle would also allow information to be easily updated with the identification of new emerging sources of funds.

Recommendation 1

- 2.39 **The Aboriginal and Torres Strait Islander Services agency should investigate cost- effective methods of compiling and publishing information about alternative sources of funding from the three levels of government. This information should be provided to Aboriginal and Torres Strait Islander Commission Regional Councils on a regular basis.**

Audit Report No. 3, 2002–2003

Facilities Management at HMAS *Cerberus*

Introduction

Background

- 3.1 HMAS *Cerberus* is a navy base situated south-east of Melbourne, Victoria. It is a major Navy training establishment that conducts initial recruit training as well as specialist category training in areas such as communications and engineering. Also located on site are the Australian Defence Force Schools of Catering and Physical Training and a major health centre for operational and training needs. In 1994, redevelopment commenced of the facilities at HMAS *Cerberus* including the construction of a new health centre.
- 3.2 In 2000, Defence's Inspector-General Division (IGD) conducted an investigation following allegations about Defence Estate Organisation's (DEO) facilities management at HMAS *Cerberus* and other Defence bases in Victoria.
- 3.3 IGD found that there were procedural and managerial deficiencies in certain DEO activities and that 'approximately half the allegations

investigated were either proven or at least supported by the available evidence'.¹

3.4 The main issues concerning facilities management at HMAS *Cerberus* were:

- problems with the design, and defects in construction, of the health centre that were not fixed by the designer or builder and were rectified largely at Defence cost;
- unresolved facilities problems, particularly those that pose health and safety concerns;
- inconsistencies in holding contractors accountable for performance, and adequate documentation and recordkeeping; and
- breaches of procurement requirements and guidelines.²

The audit

3.5 The audit was undertaken following a request to the Auditor-General from the then Minister of Defence, the Hon Peter Reith MP, to conduct an independent investigation into facilities management at HMAS *Cerberus*. The objective of the audit was to clarify issues of concern and to ensure that lessons would be learnt to assist Defence facilities management generally.³

Audit findings

3.6 Key findings from *Audit Report No. 3, 2002–2003, Facilities Management at HMAS Cerberus*, were:

- there was inadequate contract management and a lack of consistency in ensuring contractor accountability;
- poor documentation management had been a contributing factor in the problems experienced at HMAS *Cerberus*;
- management of fire safety issues had been appropriate and the electrical problems appear to have been resolved and were not an ongoing concern;

1 Inspector-General Division, Management Audit Branch, Report No. 200169, *Investigation of Allegations Made About the Defence Estate Organisation*, 13 February 2001, p. 3.

2 Auditor-General, *Audit Report No. 3, Facilities Management at HMAS Cerberus, 2002-2003*, Canberra, July 2002, p. 9.

3 Auditor-General, *Audit Report No. 3, 2002–2003*, p. 19.

- blue water⁴ had been a problem from approximately 6 months after the construction of the health centre in 1996—Defence should have taken more decisive action to address the problem earlier;
- there was no evidence to support claims of bias in awarding the Comprehensive Maintenance Contract (CMC) but that the process could have been improved to reflect better practice; and
- the Infrastructure Division (ID) did not have a formal, systemic approach to risk management in contracting.⁵

3.7 The audit also confirmed the findings from the IGD investigation.

The Committee's review

3.8 As part of its ongoing review of audit reports, the Committee decided to review *Audit Report No. 3, 2002-2003*.

3.9 At a public hearing on 28 March 2003, the Committee took evidence on the following issues:

- tender contract and management;
- follow-up of recommendations from previous reviews;
- recordkeeping;
- blue water; and
- performance reporting.

Tender contract and management

Comprehensive Maintenance Contract tendering process

3.10 In 1997, when DEO was formed, a new contract strategy was introduced to replace the existing arrangements of separate managing contractors for general building and facilities maintenance, and for fixed plant and equipment maintenance. DEO devised regional CMCs with a single managing contractor.

4 Blue water is a blue-green discolouration of water which can occur in plumbing systems. Although the cause of blue water is unclear, the corrosion of copper water pipes can result in blue water.

5 Auditor-General, *Audit Report No. 3, 2002-2003*, pp. 12-13.

- 3.11 Following allegations that DEO and a tenderer colluded during the CMC tender process, the IGD reviewed the tender process for the CMC in Victoria. Although the IGD found no evidence to support this allegation, it was clear that the tender process did not equate with best practice. Major criticisms were that:
- there was no weighting given between technical criteria and price for each tender; and
 - that tender assessments did not meet appropriate standards of probity and equity.⁶
- 3.12 In its audit, the ANAO revisited the issue and examined whether there was any evidence of bias in awarding the tender. While the ANAO also found no evidence to support the claim of biased tendering, it recommended the use of a probity adviser on future tenders for contracts of significant value. Defence agreed that \$20 million be the trigger for the use of a probity adviser.
- 3.13 At the public hearing, the Committee asked Defence what progress had been made in implementing this recommendation.
- 3.14 Defence responded that it had implemented the recommendation in two stages:
- We are on the verge of introducing a new suite of contracts which will have behind it a whole new through-life tender evaluation process which will have probity as one of the check mechanisms. That is due to come on line in the middle part of this year.
- However, that said, since the ANAO report ... we have been employing legal advisors on tender evaluation processes for all projects, whether \$20 million or above, and indeed for all disposal activity and major refurbishment activities as well. ... we have legal advisors who provide advice on probity and the steps that have been undertaken by our officers during the tender evaluation and negotiation process.⁷

Tender evaluation

- 3.15 In its audit, the ANAO found that the qualitative means of assessing the relative merits of the tendered prices in conjunction with quality were not

⁶ Auditor-General, *Audit Report No. 3, 2002–2003*, p. 44.

⁷ Mr Michael Pezzullo, *Transcript*, 28 March 2003, p. 30.

clear and left scope for uncertainty concerning the reasons for the final decision.⁸

3.16 The ANAO recommended that that Defence use a suitable methodology for assessing contract tenders to ensure that technical and pricing factors are appropriately combined to achieve an objective decision and best value for money.⁹

3.17 In response, Defence agreed with qualification to this recommendation. It commented:

Facilities contracts are relatively simple and are usually fixed price lump sum contracts, with schedules of rates where necessary. Therefore, there are very few occasions requiring extensive pricing comparison of multiple components of a tender.¹⁰

3.18 The Committee sought comments from ANAO as to whether it accepted this qualification.

3.19 The ANAO stated:

As [the audit] report points out, in the assessing of this tender it was quite difficult to come along subsequently and understand just how the tender evaluation group made its decisions. It would have been much better to have a refined methodology that the tender group could follow easily and that [the ANAO] could audit easily.¹¹

3.20 However, Defence responded:

The tender evaluation plans for major construction developments of this nature as well as tender evaluation plans for ongoing comprehensive maintenance contract would ... be unrecognisable from the sort of documentation that would have been available from 1994-95 onwards ...

[The tender evaluation plans and reports] have a far more auditable quality about them ... I would contend that there is a pretty strong auditable trail these days that eight or nine years ago, as the auditors have found, would be very hard to reconstruct.¹²

3.21 The ANAO conceded that:

8 Auditor-General, *Audit Report No. 3, 2002–2003*, p. 13.

9 Auditor-General, *Audit Report No. 3, 2002–2003*, p. 47.

10 Auditor-General, *Audit Report No. 3, 2002–2003*, p. 47.

11 Mr Warren Cochrane, *Transcript*, 28 March 2003, p. 35.

12 Mr Michael Pezzullo, *Transcript*, 28 March 2003, p. 35.

... the system is getting better and there is more strategy in the way that the now Infrastructure Division is approaching its contracting. [The ANAO] would not say that everything is perfect yet, but it has come a long way since 1994–95.¹³

Committee comment

- 3.22 The Committee notes the improvement made by Defence in improving its tender evaluation documentation. However, the Committee considers that the tender evaluation process would be enhanced by a consistent tender evaluation methodology as recommended by the ANAO.

Follow-up recommendations from previous reviews

- 3.23 On numerous occasions, the Committee has expressed concern about Defence's follow-up of IGD, ANAO and JCPAA recommendations. In 2001, the Committee noted that Defence is:

... putting in place controls to ensure that recommendations made by the ANAO, Defence internal audit and the JCPAA are routinely monitored. The Committee expects the implementation of follow-up mechanisms to systematically report on outstanding recommendations which have not been implemented.¹⁴

- 3.24 The IGD has established the Audit Recommendations Management System (ARMS) in order to monitor the implementation of recommendations.

- 3.25 However, the audit found that recommendations from the IGD investigation of facilities management in 2000 had not been placed on ARMS. The audit report noted that:

... their absence from ARMS made it more difficult to establish their status and to track the progress in their implementation.¹⁵

- 3.26 The audit report also noted that:

... better practice would indicate that the recommendations [including ANAO and JCPAA recommendations] should be formally recorded on a system such as ARMS to ensure that their

13 Mr Warren Cochrane, *Transcript*, 28 March 2003, pp.35–6.

14 JCPAA, *Report 385, Review of Auditor-General's Reports 2000–2001, Second and Third Quarters*, August 2001, p. 38.

15 Auditor-General, *Audit Report No. 3, 2002–2003*, p. 36.

implementation is kept under review by senior management and the Defence Audit Committee.¹⁶

3.27 The Committee sought confirmation from the Inspector-General as to the formal mechanisms in place to respond to recommendations and whether there was a system of monitoring to ensure that Defence was acting on what had been agreed.

3.28 The Inspector-General told the Committee that recommendations are placed on ARMS by his auditors. In relation to monitoring, the Inspector-General advised the Committee that:

The defence audit committee ... regularly takes a snapshot of active recommendations and the recommendations that have been completed. It does that pretty much every six weeks ... it meets about 10 times a year.¹⁷

3.29 The Committee was also advised that a sample check of high priority recommendations (including ANAO and JCPAA recommendations) had been carried out to ensure that those recommendations that are marked as 'complete' on the system had been in fact implemented.¹⁸

3.30 The Inspector-General discovered that:

... people were marking things 'complete' simply because the due date was coming up, not because they had actually completed them.¹⁹

3.31 As well, there were instances of problems when implementation of a recommendation involved several parties. Sometimes one party marked the recommendation as 'complete' on ARMS because it had completed its contribution and forwarded responsibility for completion of the recommendation to the next party. Consequently, certain stages of implementation were complete, but the overall intent of the recommendation was not.²⁰

Committee comment

3.32 Although Defence has introduced ARMS to record progress in implementing the recommendations to which Defence had agreed, it is clear that the system is not being used appropriately.

16 Auditor-General, *Audit Report No. 3, 2002–2003*, p. 36.

17 Mr Claude Neumann, Inspector-General Defence, *Transcript*, 28 March 2003, p. 31.

18 Inspector-General Defence, *Transcript*, 28 March 2003, p. 32.

19 Inspector-General Defence, *Transcript*, 28 March 2003, p. 32.

20 Inspector-General Defence, *Transcript*, 28 March 2003, p. 32.

Recommendation 2

- 3.33 **The Department of Defence should immediately update its Audit Recommendations Management System and provide the Committee and the Australian National Audit Office with a report on the current status of all Committee and Audit Office recommendations.**
- 3.34 The Committee expects Defence to review its instructions concerning the use of ARMS and its monitoring arrangements to ensure that the system is being correctly used to monitor Defence's progress in completing the requirements of the recommendations to which it has agreed.

Recordkeeping

- 3.35 In recent years, recordkeeping in Commonwealth organisations has been a recurring issue in ANAO audits. Many audits have noted an absence of, or only limited, ongoing documentation or records. In some instances, the level of documentation available was insufficient to evidence and support administrative actions and decision-making processes.²¹
- 3.36 A recent ANAO audit into recordkeeping noted that
... recordkeeping is an essential enabler in any organisation's corporate governance and critical to accountability.²²
- 3.37 In its internal investigation, the IGD found that DEO Project Delivery officers were unable to provide IGD with the complete set of relevant files for projects at HMAS *Cerberus* and therefore the IGD could not reach a detailed conclusion in regard to the criticisms. IGD also found that there was no efficient system in place to locate contract documentation.²³
- 3.38 The ANAO, in its audit, agreed that poor documentation management in DEO contributed to facilities management problems at HMAS *Cerberus* and had made it difficult for IGD to investigate the issues.²⁴

21 Auditor-General, *Audit Report No. 45, 2001–2002, Recordkeeping*, Canberra, May 2002, p. 11.

22 Auditor-General, *Audit Report No. 45, 2001–2002*, p. 11.

23 Auditor-General, *Audit Report No. 3, 2002–2003*, p. 32.

24 Auditor-General, *Audit Report No. 3, 2002–2003*, p. 32.

- 3.39 The Committee asked Defence what had been done to improve document handling and file management procedures as recommended by the IGD.
- 3.40 Defence told the Committee that there was now a requirement for all documents to be cross-referenced into the electronic database system, Defence Estate Management System (DEMS). Defence had also begun to explore the feasibility of integrating DEMS and the Defence Records Management System to create a paperless office system. As Defence explained:

The DEMS system ... is fully functional in tracking works against invoices ... The next stage in that process is enabling the reference system to open the document itself, so that everyone will be able to operate in a fully paperless way ... That is part of a bigger Defence-wide project.²⁵

Committee comment

- 3.41 The Committee notes the progress that Defence has made with regards to its recordkeeping and expects Defence to maintain momentum in this area.

Blue water

- 3.42 Blue water is a blue-green discolouration of water which can occur in plumbing systems. Although the cause of blue water is unclear, the corrosion of copper water pipes can result in blue water.²⁶
- 3.43 Blue water was first observed at the health centre approximately six months after the completion of construction in 1996. While attempts to rectify the problem had begun in December 1996, there was no action taken between June 1997 and April 1999. At the time of the audit, it was still a problem.
- 3.44 In its internal audit, the IGD investigated allegations that DEO did not hold contractors accountable for poor performance on facilities project work at HMAS *Cerberus* including concerns with blue water affecting the health centre's water.
- 3.45 In its audit, the ANAO found that as the cause of blue water was unclear, and it was difficult to apportion the cause of the problem at the health centre to poor contractor performance. This was particularly so, because

25 Mr Michael Pezzullo, *Transcript*, 28 March 2003, p. 34.

26 ActewAGL, *Blue Water and Copper Corrosion*, [www.actewagl.com.au]

blue water had been found in other buildings at HMAS *Cerberus* where the contractors of the health centre had not been working.²⁷

3.46 The audit also found no firm evidence of advice to staff on the blue water problem prior to August 2001, although anecdotal evidence indicated that the staff were aware of the problem.²⁸

3.47 The ANAO concluded that more decisive action should have been taken by Defence to remedy the problem earlier.²⁹

3.48 During the public hearing, the Committee raised various issues with Defence including:

- the length of time it had taken to respond to the issue of blue water at HMAS *Cerberus*;
- the health risk associated with drinking blue water and whether advice had been given to personnel not to consume the water; and
- why the action that was taken in the end to rectify the blue water problem (i.e. replacing of the pipes) was not taken in the first place.

3.49 In respect to these three issues, Defence responded:

- the blue water had been tested at length by various engineering consultants and the problem was not as simple as first assumed;³⁰
- that once the defect became apparent, immediate action was taken to notify the staff and bottled drinking water was provided at the health centre;³¹ and
- from an audit and value-for-money view, it was felt necessary to attempt to identify any localised source of the problem before replacing all the plumbing—in the event testing had proved inconclusive.³²

3.50 The Inspector-General supported the comments made by Defence with regards to the remedial action taken; commenting that the problem was easier to deal with in hindsight.³³

27 Auditor-General, *Audit Report No. 3, 2002–2003*, p. 26.

28 Auditor-General, *Audit Report No. 3, 2002–2003*, p. 41.

29 Auditor-General, *Audit Report No. 3, 2002–2003*, p. 42.

30 Mr Michael Pezzullo, *Transcript*, 28 March 2003, pp. 30, 34.

31 Mr Michael Pezzullo, *Transcript*, 28 March 2003, p. 34.

32 Mr Michael Pezzullo, *Transcript*, 28 March 2003, p. 34.

33 Inspector-General Defence, *Transcript*, 28 March 2003, p. 34.

Committee comment

- 3.51 The Committee notes that at the time of the audit, the copper pipes in the health centre as well as in the accommodation buildings affected by blue water were being replaced.
- 3.52 The Committee notes there was a significant delay between June 1997 and April 1999 in addressing the problem. The Committee considers that such a delay where health issues are concerned is not acceptable and should not be repeated.

Performance monitoring

- 3.53 In its audit report, ANAO recommended that Defence put in place a timetable for the implementation of appropriate performance monitoring devices for plant and equipment that service buildings. These devices should be activated at the earliest practical date.³⁴
- 3.54 The Committee sought clarification with regards to this recommendation.
- 3.55 Defence stated that there were two sub disciplines within facilities management:
- ... there is what is called fixed plant and equipment ... that helps your run a building, such as the power systems, the elevator systems and the air conditioning etc. General building maintenance and upgrades relate to the physical fabric of the building, such as broken windows that are replaced and the replacement of casings for lighting systems etc. Fixed plant and equipment, if not regularly monitored, obviously creates a cost down the line in terms of major overhauls of your air conditioning system, your elevator systems and the fuel installations that are associated with your facilities.³⁵
- 3.56 Defence advised the Committee that it had begun implementing the ANAO's recommendation:
- The way we are accomplishing [the recommendation] is to introduce performance monitoring requirements for our comprehensive maintenance contractors ... we monitor them by

34 Auditor-General, *Audit Report No. 3, 2002–2003*, p. 50.

35 Mr Michael Pezzullo, *Transcript*, 28 March 2003, p. 36.

having [key performance indicators] over the top of them that they are required to comply with.³⁶

Asset management

3.57 During the hearing, the Committee expressed concern over Defence's ability to manage its assets. This view has arisen due to Defence's performance in this area which had been exposed by previous Committee inquiries.

3.58 In response, Defence stated that with regards to the estate, the Defence Estate Management System (DEMS) was a fully IT enabled system which could capture fixtures and structures on the estate as well as providing details such as room sizes and the number of chairs and tables in each room. Defence added:

... whilst [DEMS] is not as mature as the technology probably allows, I suspect it is probably better than most public bureaucracies around the world, to the extent that we have embedded UK [Ministry of Defence] officers trying to learn from us how we have pulled that together.³⁷

3.59 The Committee sought comment from the Inspector-General. He responded:

I think it is about management issues rather than simply systems issues. I think [the ANAO] was right in saying that the changeover in management to Infrastructure Division from Defence Estate has made a whole lot of things different. The whole approach is different.³⁸

Committee comment

3.60 The Committee acknowledges the change in approach to asset management since the changeover from Defence Estate to the Infrastructure Division. However, the Committee considers there remains scope for continuous improvement.

36 Mr Michael Pezzullo, *Transcript*, 28 March 2003, p. 36.

37 Comments made at the public hearing by Defence were in regards to Estate Management only. Weapons equipment and systems are managed by DMO. See Defence, *Transcript*, 28 March 2003, pp. 36–7.

38 Inspector-General Defence, *Transcript*, 28 March 2003, p. 37.

Audit Report No. 7, 2002–2003

Client Service in the Child Support Agency Follow-up Audit

Introduction

Background

4.1 The Child Support Scheme (the scheme) was established in 1988 as a national system for transferring child support payments between separated parents for the benefit of their children. The Child Support Agency (CSA) leads the administration of the scheme. Its main functions are to:

- register and assess cases;
- collect payments if requested;
- enforce child support liabilities; and

- provide information on child support matters.¹
- 4.2 The CSA operates in a complex and sensitive environment. The strong emotions often felt by separated parents and their experiences with other aspects of the separation process can have a serious impact upon their relationship with the CSA.
- 4.3 The CSA administered over 650 000 child support cases as at June 30 2002.² This figure included approximately 330 000 cases for which the CSA was the collection agency, that is, where the CSA collected and disbursed child support payments. Each case has two CSA clients—a payer and a payee—so that the CSA had approximately 1.3 million clients at the time, as well as responsibility for around 990 000 children.
- 4.4 The CSA has been subject to a number of audits and parliamentary reviews during the 1990s. In particular, the 1997–98 ANAO audit of the CSA that examined the administration of the scheme and made 12 recommendations to enhance the CSA’s performance.³ The audit report was further reviewed by the Committee, which reinforced the audit findings with three additional recommendations in *Report 367, Review of Auditor-General’s Reports 1997–98*.

The audit

- 4.5 The objectives of the audit were to:
- assess the CSA’s implementation of the 12 recommendations contained in the previous ANAO audit and 3 recommendations pertaining to it in the Committee’s *Report 367*; and
 - establish whether the CSA had improved the management and delivery of its client service, taking into account the recommendations and findings detailed in the above reports as well as appropriate alternative measures and emerging issues that had affected the agency.
- 4.6 The audit did not assess the impact of the CSA’s redeveloped IT system (CUBA) on client service, as fieldwork was completed before the introduction of the new system in March 2003. Nor did it address policy issues relating to the scheme such as the child support formula, as these issues were outside the audit mandate of the ANAO.

1 Auditor-General, *Audit Report No. 7, 2002–2003, Client Service in the Child Support Agency Follow-up Audit*, Canberra, September 2002, p. 11

2 Auditor-General, *Audit Report No. 7, 2002–2003*, p. 11.

3 Auditor-General, *Audit Report No. 39, 1997–98, Management of Selected Functions of the Child Support Agency*, Canberra, April 1998.

Audit findings

- 4.7 The audit found that the CSA had placed a strong emphasis on addressing the issues and recommendations of the previous ANAO audit and the associated Committee report. The CSA had either fully or substantially implemented almost all of the 15 combined recommendations. This had been achieved in an integrated manner, applying a holistic approach that implemented the recommendations as part of a fundamental restructure of CSA business.⁴
- 4.8 The ANAO also found that the restructure, particularly the Client Service Model and the CSA's new stream structure (comprised of New Clients, Collection Support, and Debt Management Services) had significantly improved the management of its business as had the enhancement of support for staff at the CSA. As a result the ANAO noted an increase in performance since its previous report.⁵
- 4.9 The report also noted areas where improvements could be made in several areas, including:
- the provision of more accurate advice by the CSA to clients;
 - clearer explanation to clients of decisions taken by the Agency;
 - ensuring that obligations made by staff were fulfilled;
 - the application of case-locking rules (whereby the Agency ensures that a client's case issues are referred to one Case Support Officer); and
 - many aspects of the Change of Assessment process.⁶
- 4.10 In addition, the audit report also identified the need for improvement in the management of client debt. The report noted that the magnitude and timeliness of payments remained a problem for many CSA Collect payees, who are owed an average of over \$2100 at 30 June 2001.⁷
- 4.11 The ANAO suggested gains could be made in the following areas:
- reviewing procedures for employer withholding of current payments and employer withholding of arrears;
 - revision of performance measures of debt and collection;
 - refining case selection criteria for Individual Case Management ; and

4 Auditor-General, *Audit Report No. 7, 2002–2003*, p. 12.

5 Auditor-General, *Audit Report No. 7, 2002–2003*, p. 12.

6 Auditor-General, *Audit Report No. 7, 2002–2003*, p. 13.

7 Auditor-General, *Audit Report No. 7, 2002–2003*, p. 13.

- improving the capacity for cases to be referred from the New Clients Stream to the Debt Management Services Stream (referred to as cross stream referral).⁸

4.12 The ANAO report acknowledged the genuine commitment on the part of the CSA to making continual improvements in its processes and recognised the nature of the sensitive environment in which the CSA operated.

The Committee's review

4.13 On 28 March 2003, the Committee held a public hearing to review the progress made by the CSA in relation to the implementation of the ANAO's recommendations.

4.14 The Committee took evidence on the following issues:

- implementation of previous recommendations;
- complaints handling and performance;
- determination of assessable income; and
- debt management and collection.

Implementation of previous recommendations

4.15 The CSA was the subject of a performance audit by the ANAO in 1997–98. That report, entitled *Management of Selected Functions of the Child Support Agency*, contained 12 recommendations to enhance the CSA's performance. The CSA agreed with all 12 recommendations.

4.16 During 1998, the Committee reviewed *Audit Report No. 39, 1997–98* and concluded that it expected 'further improvement in performance management, through the continued implementation of the ANAO's recommendations'.⁹

4.17 In addition, the Committee strengthened the ANAO's view with three additional recommendations. These recommendations were:

- **Recommendation 2:** ... the [Child Support Agency] should take immediate action to simplify the language and style used in its

⁸ Auditor-General, *Audit Report No. 7, 2002–2003*, p. 13.

⁹ JCPAA, *Report 367, Review of Auditor-General's Reports 1997–98*, Canberra, March 1999, p. 60.

publications and should employ an outside consultant to undertake the task.

- **Recommendation 3:** The Child Support Agency should commission an expert consultant to undertake comprehensive and regular client surveys in order to determine the level of client awareness of the Charter and complaints service.
- **Recommendation 4:** To ensure equitable outcomes are delivered, the CSA should take prompt action to ensure that the setting of levels of Employer Withholding of Arrears reflect the annual income of the client.¹⁰

- 4.18 The 2002–2003 audit report found that the CSA had either ‘fully, substantially or partially implemented all the recommendations of the previous ANAO audit and associated JCPAA report’ or that the CSA had adopted an alternative strategy. The ANAO considered that the CSA had understood and responded to the intent of these external reviews. However, the ANAO noted that some of the recommendations had not been implemented as fully as may have been expected.¹¹
- 4.19 The Committee sought clarification of the extent to which its recommendations had been implemented, particularly focussing on Recommendation 3 (see above).
- 4.20 The Committee expressed concern that although an Executive Minute¹² had been received from the relevant department (Department of Family and Community Services) stating that this recommendation had been implemented, the ANAO report had revealed that the CSA had measured its performance in meeting charter commitments rather than measuring clients awareness of the charter.¹³
- 4.21 The CSA responded that it had implemented the intent of the recommendation while conceding that this was different from implementing the exact recommendation. It considered its position was more meaningful to its clients:

We try and put ourselves in the shoes of our clients. If you ask a client the question, ‘Are you aware of the Child Support Agency’s client service charter?’ I think they will inevitably say, ‘What’s that?’ ... That is because it does not necessarily have any meaning for them ... Rather than ask clients the specific question, ‘Are you

10 JCPAA, *Report 367*, Recommendations 2, 3, 4, pp. 48, 51, 59.

11 Auditor-General, *Audit Report No. 7, 2002–2003*, p. 116.

12 Hon Larry Anthony MP, Minister for Community Services, *Executive Minute on JCPAA Report 367*, 14 October 1999.

13 *Transcript*, 28 March 2003, p. 16.

aware of the charters?’ we asked them, ‘How do you think the agency is performing in relation to [the] objectives [of the charter]?’¹⁴

4.22 However, the Committee considered that the CSA had failed to understand the purpose behind the Committee’s recommendation. Client awareness of the CSA’s charter would include awareness of CSA problem resolution processes. This would increase use of those avenues before dissatisfied clients approached Members of Parliament with problems.¹⁵

4.23 The Committee also noted that the ANAO was dissatisfied with the CSA’s implementation of Recommendation 4 from *Report 367* in spite of assurances from the CSA that the recommendation had been implemented. The recommendation was that:

To ensure that equitable outcomes are delivered, the CSA should take prompt action to ensure that the setting of levels of Employer Withholding of Arrears reflects the annual income of the client.¹⁶

4.24 The ANAO’s view was that the CSA had not successfully addressed the problem referred to in the recommendation. Its analysis showed that much of the estimation of arrears to be withheld was still based on the size of the debt rather than on the capacity to pay or annual income. The audit report stated:

The employer rates applied to debtors under garnishees arrangements did not appear to fully reflect debtor capacity to pay. In February 2002, the average [Employer Withholding of Arrears] deduction for debtors with income of less than \$20 000 was actually higher than for debtors with incomes of more than \$20 000.¹⁷

4.25 A significant issue was the lack of research by the CSA to analyse what, if any, improvement had been made in this area. Analysis would have shown that there was no improvement over time and therefore no effective implementation of Recommendation 4.

4.26 The CSA responded by assuring the Committee that it had again reviewed guidance to staff making assessment of Employer Withholding of Arrears (EWA). It conceded that previous guidelines for staff had been too vague and that since the ANAO report, the CSA had implemented more detailed

14 Ms Catherine Argall, *Transcript*, 28 March 2003, p. 16.

15 *Transcript*, 28 March 2003, p. 17.

16 JCPAA, *Report 367*, p. 59.

17 Auditor-General, *Audit Report No. 7, 2002-2003*, p. 22.

guidelines for assessing the level of EWA. These guidelines included a 'ready reckoner' as a tool for staff making such judgements.

- 4.27 The CSA indicated that it was very concerned with assessing clients accurately in relation to the EWA to be applied and that it was committed to providing more training and development to the staff making these decisions. The CSA believed progress had already been made in this area and the ANAO endorsed the new guidelines as having 'clearer criteria for capacity to pay decisions for allocating debt repayments.'¹⁸

Committee comment

- 4.28 The Committee notes that the CSA has no separate process, outside of ongoing business arrangements, for monitoring the implementation of recommendations from external reviews.
- 4.29 The Committee is concerned by the tendency of the CSA to re-interpret the recommendations of both the JCPAA and the ANAO. This may have led to delays in improving the system, which in turn meant a less fair and efficient system for CSA clients. The Committee considers that its recommendations and those of the ANAO are sufficiently well-thought out and considered to warrant full implementation.
- 4.30 If the CSA disagrees with the recommendations of external reviewers it should make its concerns explicit to both its Minister and those reviewers. To do otherwise potentially misleads its Minister and (when Committee recommendations are involved) the Parliament.
- 4.31 To achieve the improvement necessary to ensure an equitable application of EWAs, the Committee considers that the CSA will need to be vigilant regarding the application of criteria used by staff to determine EWAs. Such vigilance could be achieved through the CSA's internal audit mechanism.

Recommendation 3

- 4.32 **The Child Support Agency should advise the Joint Committee of Public Accounts and Audit of the Agency's progress towards implementing the recommendations directed to it in *Report 367, Review of Auditor-General's Reports 1997-98, Third Quarter*.**

18 Mr Andrew Morris, *Transcript*, 28 March 2003, p. 18.

Complaints handling and performance

- 4.33 The complaints process within the CSA has long been a problematic area for the agency. The audit report examined the efficacy of the implementation of Recommendation 3 in relation to client awareness of the complaints process as well as measuring the performance of the complaints process itself.
- 4.34 The Committee sought further explanation of how the CSA measured client awareness of the complaints service, as this was an area in Recommendation 3 in which there was dispute over the full implementation.
- 4.35 The CSA acknowledged that its internal surveys did not actually measure the level of client awareness of the complaints process. It continued with clarification of how it promoted awareness of the complaints process.
- 4.36 The CSA suggested that its promotion of the complaints process was quite comprehensive. The agency used various strategies to ensure that clients and the general public knew of the complaints process available to them. These included:
- the issuing of an information kit to all new clients which contained a pamphlet about the complaints process;
 - the inclusion of the same pamphlet with all new assessment notices, issued every 12-15 months;
 - use of the CSA website to explain and promote the complaints process; and
 - a separate listing in the *Telstra White Pages* for CSA Complaints service.¹⁹
- 4.37 The CSA added that it comprehensively monitored complaints received either directly or through external agencies. It considered that one measure of complaints process awareness was the number of complaints coming direct to the agency. As this figure had increased since the previous ANAO report, the CSA concluded that it was improving client awareness of the complaints service.²⁰
- 4.38 The CSA detailed the process involved when it addressed complaints. This was a three stage process, where clients began with their own case
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19 Ms Sheila Bird, *Transcript*, 28 March 2003, p. 19.

20 Ms Sheila Bird, *Transcript*, 28 March 2003, p. 19.

officer, then progressed to the team leader for that officer. If the complaint remained unresolved, a client had the option of utilising the services of an independent complaints officer. The agency noted that, in all complaints cases it tried 'to identify the broader systemic issues' and address these in its staff training.²¹

4.39 The CSA advised that the percentage of upheld complaints was between 17 and 20 per cent, while also noting that not all upheld complaints resulted in a change to child support. However, the CSA emphasised that complaints might result in an apology or compensation or in a significant change to the system.²²

4.40 The CSA acknowledged that complaints were an ongoing issue for the agency but indicated the nature of the work meant that this was inevitable:

This is an area, you will appreciate, that no matter how well we deliver a child support service there will continue to be those parents who are unhappy with the service. Our research suggests that as many as 15 per cent of the overall case load may well be a group of clients that we will fail to satisfy regardless of what we do.²³

4.41 The CSA also noted that approximately 90 per cent of all separated parents currently use the CSA to assess their child support. Of that 90 per cent, about 50 per cent of parents had an annual assessment and completed the financial transfer directly between themselves. The agency made the point that as the parents who were able to manage their own payments were removed from the CSA client pool, the agency was left with a group of parents who 'are the ones who cannot agree.'²⁴

Committee comment

4.42 The Committee is pleased to note that the CSA has demonstrated a genuine determination to improve the awareness of its complaints service, as well as monitoring how effective the agency was in receiving complaints directly from clients rather than via an external agency. That progress is being made is supported by findings in the ANAO report that

21 Ms Catherine Argall, *Transcript*, 28 March 2003, p. 26.

22 Ms Sheila Bird, *Transcript*, 28 March 2003, pp. 25–6.

23 Ms Catherine Argall, *Transcript*, 28 March 2003, p. 19.

24 *Transcript*, 28 March 2003, p. 20.

complaints through the Commonwealth Ombudsman and Members of Parliament had declined substantially between 1997–98 and 2000–01.²⁵

- 4.43 The Committee acknowledges the sensitivity of the environment within which the CSA operates and acknowledges the efforts at improving systems and staff support since the previous audit report in 1997–98.
- 4.44 However, the Committee notes that in dealing with an area as sensitive as parental separation and child support, the agency must maintain high levels of vigilance and be continually seeking ways of improving its performance.

Determination of assessable income

- 4.45 The Committee focused on the determination of assessable income in cases where non-custodial parents hide assets, for example by structuring their finances to reduce their assessable income or by moving assets offshore and having offshore bank accounts.
- 4.46 Committee members noted that this was an issue of serious contention among their constituents and one about which they regularly received representations.
- 4.47 The CSA explained that in circumstances where the parent in receipt of child support (the payee parent) believed that the assessment for the paying parent was not commensurate with their capacity to pay, there was the option of requesting a change of assessment. In this instance payee parents were able to seek a determination of child support that was not based on the standard formula but was more reflective of the paying parent's capacity to pay.
- 4.48 This process arose from a legislative power that came into force in 1999, called a registrar initiated change of assessment.²⁶ The CSA explained the benefits of the power:

This is where the registrar initiated change of assessments is an extraordinarily beneficial power ... we explore all of the information where information from a payee and/or other source indicates that there are assets which seem to have disappeared ... we can track some of the information, include it in affidavits that we build then take those cases to a court, enabling a judge to look

25 Auditor-General, *Audit Report No. 7, 2002–2003*, p. 68.

26 Ms Catherine Argall, *Transcript*, 28 March 2003, p. 20.

at the overall circumstances of a particular client and then make a judgement about whether in fact this person has a capacity to pay that is not currently reflected and whether there should be an enforcement summons.²⁷

4.49 The CSA reported that the registrar initiated change of assessment had been a very successful tool for use in situations where there were disputes about capacity to pay. The agency added that part of the reason was that 'the court does not have to have 100 per cent proof that the person has assets overseas to make a particular order'.²⁸ Allowing this discretion in determination of assessment provided a limited safeguard for payee parents who were being disadvantaged by the application of a standard formula of assessment.

4.50 The ANAO report referred generally to the change of assessment function and stated:

By its nature, a contentious atmosphere surrounds the change of assessment function, with much of the client satisfaction related to broader child support scheme issues and outcomes.²⁹

4.51 The audit report also noted the high cost involved in any change of assessment process as well as the heavy workloads and tight timelines within which the CSA had to research, determine and finalise cases.

Committee comment

4.52 The Committee recognises that many custodial and non-custodial parents face financial difficulties, especially after starting new families. Unfortunately, the CSA from time to time has to deal with cases where its clients may not always be completely reliable. The Committee considers that while the CSA has undertaken to develop procedures to investigate cases of discrepancy between actual and apparent capacity to pay, it is incumbent upon the agency to ensure that its clients understand the options of determining a new assessment.

4.53 The Committee notes that Members of Parliament still receive a great many complaints about the CSA and in particular about the potential for paying parents to hide income to influence the child support liability assessment, and on the other hand about the financial hardships faced by non-custodial paying parents. The Committee urges the CSA to examine

27 Ms Catherine Argall, *Transcript*, 28 March 2003, p. 21.

28 Ms Sheila Bird, *Transcript*, 28 March 2003, p. 22.

29 Auditor-General, *Audit Report No. 7, 2002-2003*, p. 83.

some of the opportunities for improving the change of assessment process as detailed in the ANAO report.³⁰

Debt management

4.54 Child support debts are incurred whenever liable parents do not meet their obligations. The ANAO report noted that:

Such debt is a significant issue for the Commonwealth and the community because it means that children have not received the child support entitlements and parents have not met their share of the cost of supporting their children. Child support debt also tends to undermine the confidence of carer parents in the operation of the scheme.³¹

4.55 The Committee was concerned at the ANAO's opinion that the magnitude of arrears and timeliness of payments remained a problem for the CSA. The Committee sought clarification from the CSA about strategies taken by the agency to 'manage debt at an early stage before it starts to escalate'.³²

4.56 The CSA agreed that debt management was of major concern to the agency. It explained that the recent increase in debt arose from the introduction in 1999 of a minimum annual child support payment of \$260. The introduction of this payment had caused many CSA Collect payers to have small debts. This evidence was supported by the findings of the audit report which noted that:

The effect of the minimum-liability legislation was to sharply increase the number of cases with small ongoing liabilities and small debts. The percentage of payers with child support debts of under \$500 rose from 22 per cent in June 1999 to 38 per cent in June 2001. Largely as a result of this, the overall percentage of payers who had debts rose from 56 per cent in June 1997 to 74 per cent in June 2001.³³

4.57 In spite of this, CSA also acknowledged that there were a small percentage of clients, around five per cent, with very large debts of more than \$10 000. The ANAO report noted that these debts were very likely to be

30 Auditor-General, *Audit Report No. 7, 2002–2003*, pp. 81–2.

31 Auditor-General, *Audit Report No. 7, 2002–2003*, p. 84.

32 *Transcript*, 28 March 2003, p. 26.

33 Auditor-General, *Audit Report No. 7, 2002–2003*, p. 85.

‘unrecoverable because of the size and age and the limited financial capacity of many debtors.’³⁴

- 4.58 The CSA explained some of its strategies to improve debt management. These included a new organisational structure under which CSA Collect clients were grouped and serviced.
- 4.59 In the new structure a New Clients Services stream focused on building the capacity of parents to manage their child support arrangements. Triggers for agency concern had also been introduced. These included first time default reports, and the capacity to refer for priority attention, clients who appeared likely to become non-compliant and therefore likely to accumulate debt.
- 4.60 The Committee also canvassed the interplay between Centrelink and the CSA in the debt management process, expressing concern that in receiving arrears the payee may unwittingly incur a family tax benefit debt.
- 4.61 The CSA explained the legislative relationship whereby Centrelink may share information with the CSA where that information is necessary for the CSA to fulfil its functions:
- Some of the core data around a child support case is relevant to both CSA and Centrelink in that, after we collect child support, and even when we make an assessment of child support, we actually send electronic files to Centrelink so they can make the necessary adjustments to the family tax benefit.³⁵
- 4.62 However, CSA conceded that when people received a large amount of child support arrears, the agency could do little more than suggest that the client contact Centrelink to discuss the implications. There was no capacity for spreading the arrears over a period of time as legislation demanded immediate disbursement by the CSA.
- 4.63 The ANAO report noted the increase in difficulty faced by the CSA in managing clients with debts problems due to the increase in the proportion of private collection arrangements. This increase meant that ‘the remaining pool of CSA Collect cases has on average become more difficult to manage and more likely to be non-compliant and have child support debt.’³⁶

34 Auditor-General, *Audit Report No. 7, 2002–2003*, p. 86.

35 Auditor-General, *Audit Report No. 7, 2002–2003*, p. 22–3.

36 Auditor-General, *Audit Report No. 7, 2002–2003*, p. 86.

Committee comment

- 4.64 The Committee acknowledges the ANAO's finding that the CSA had improved debt management since the previous audit in 1997–98.
- 4.65 The Committee's view is that debt management is an issue with broad financial and social implications. Child support debt means that CSA resources are required to pursue debt. As well, there is a potential impact on social security payments for carer benefits. The social impact of child support debt means that children are not being adequately supported by their parents, which may have implications for the health, housing and education of these children.
- 4.66 The Committee is pleased to note that since the implementation of CUBA, the CSA's redeveloped IT system, the agency has seen improvements in all areas of debt management and collection. The Committee looks forward to seeing a general trend of refining processes to achieve the most efficient, effective and equitable outcomes for all stakeholders.

Recommendation 4

- 4.67 **The Committee recommends that the Child Support Agency make a detailed report to the Committee on progress made in implementing new strategies to address debt management for clients of the Child Support Agency.**

Audit Report No. 18, 2002–2003

Management of Trust Monies

Introduction

Background

- 5.1 A trust exists when a person who has legal ownership of property (the trustee) is obliged to deal with that property not for the trustee's own benefit, but for the benefit of another person (the beneficiary) or for the advancement of certain purposes permitted by law.
- 5.2 The Commonwealth receives and manages certain monies in trust for other parties. As a trustee, the Commonwealth is subject to those provisions of the *Financial Management and Accountability Act 1997* (FMA Act) that deal with public money and trust money (which under the FMA Act is defined as 'special public money'). The Commonwealth is also bound by the applicable trustee legislation of the States and Territories and by the requirements of general trust law, trust deeds and special instructions issued by the Minister for Finance or his delegates.

- 5.3 Trust monies are required to be separately reported in the annual financial statements of Commonwealth organisations but are not recognised as assets of the reporting organisation because they are not available for the use or benefit of the Commonwealth. At 30 June 2001, the Commonwealth reported almost \$500 million as being held in trust.¹

The audit

- 5.4 The audit was a Business Support Process audit which examines business and financial processes in the Commonwealth. Five Commonwealth organisations were selected by the ANAO:
- the Department of Defence (Defence);
 - the Australian Securities and Investment Commission;
 - the Aboriginal and Torres Strait Islander Commission (ATSIC);
 - the Federal Court of Australia (Federal Court); and
 - the Health Insurance Commission.
- 5.5 The objectives of the audit were to:
- assess whether selected Commonwealth organisations were managing trust monies in accordance with legal and administrative requirements and better practice principles;
 - identify better practices in the management of trust monies; and
 - recommend improvements in the controls and practices relating to the management of trust monies.²

Audit findings

- 5.6 The ANAO found that trust monies were not being consistently managed by the Commonwealth organisations audited in accordance with legal and administrative requirements and better practice principles.
- 5.7 In particular, there was inadequate assurance that the legal status of trust monies were correctly identified. In some instances, monies had been incorrectly identified as trust monies, and in other instances, monies which should have been identified as trust monies were being treated as some other form of public money.
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1 Auditor-General, *Audit Report No. 18, 2002–2003, Management of Trust Monies*, Canberra, November 2002, p. 9.

2 Auditor-General, *Audit Report No. 18, 2002–2003*, p. 10.

- 5.8 Consequently, where monies were incorrectly considered to be trust monies, the Commonwealth lost potential interest earnings because it did not have access to the funds for investment. Where organisations had failed to identify monies as being trust monies, the Commonwealth was exposed to a number of risks, including not acting in accordance with the terms of a legally binding trust agreement.³
- 5.9 The ANAO made four recommendations to which the audited agencies agreed, or agreed in principle.⁴

The Committee's review

- 5.10 Three of the five audited agencies and the ANAO were invited to give evidence to the Committee at a public hearing on Wednesday, 30 April 2003. The audited agencies were:
- Defence;
 - the Department of Finance and Administration (Finance);
 - ATSIIC; and
 - the Federal Court.
- 5.11 The Committee took evidence on the following issues:
- the classification of trust accounts;
 - Comcare's compensation payments to agencies.

Classification of trust accounts

- 5.12 The audit found that Commonwealth entities appeared confused when they classified the accounts they held. ANAO told the Committee that it had determined the legal status of 19 special accounts disclosed as trusts held by the five agencies audited. Only 4 were definitely trusts and an additional 2 were unclear as to their legal status.⁵
- 5.13 A legal trust exists when:

... a person who has legal ownership of property (the trustee) is obliged to deal with that property not for the trustee's own benefit,

3 Auditor-General, *Audit Report No. 18, 2002–2003*, p. 11.

4 Auditor-General, *Audit Report No. 18, 2002–2003*, pp. 16–17.

5 Mr Trevor Burgess, *Transcript*, 30 April 2003, p. 8.

but for the benefit of another person (the beneficiary) or for the advancement of certain purposes permitted by law.⁶

- 5.14 However, the audit found that Commonwealth entities often used the words ‘trust’, ‘held in trust’, or in a ‘trustee capacity’ when referring to monies held on behalf of a third party in a vernacular rather than a legal sense. This loose use of the term may have arisen due to confusion arising from the changes to the Commonwealth’s financial framework which commenced in 1997.⁷
- 5.15 Finance explained that before the introduction of the FMA Act in 1997, the Trust Account held monies which may have been monies subject to a trust deed or monies for the government’s various businesses. Business money had to be kept in the Trust Fund because appropriations lapsed annually. In 1997 with the introduction of the FMA Act, the monies were moved to the Reserve Moneys Fund and the Commercial Activities Fund. In 1999 the introduction of accrual accounting necessitated amendments to the FMA Act and monies in the two Funds were converted into special accounts. These are ledgers in the Consolidated Revenue Fund. As before, monies in special accounts could be trust monies or monies for other purposes.⁸
- 5.16 The misclassification of monies held by the Commonwealth could result in reduced investment by the Commonwealth (when monies incorrectly thought to be in a legal trust was not invested), or the Commonwealth incorrectly deriving a benefit (when the interest on invested monies incorrectly thought to belong to the Commonwealth was not passed on to the beneficiaries).⁹ The ANAO had not attempted to quantify the effect of the misclassification on interest foregone.¹⁰
- 5.17 The ANAO recommended that where agencies were uncertain regarding the legal status of monies reported as trusts, they should obtain legal advice.¹¹
- 5.18 Finance advised the Committee that it had written to the Chief Finance Officers in all departments drawing attention to the findings of the audit report. As a result a ‘few agencies’ had consulted Finance on the matter.

6 Auditor-General, *Audit Report No. 18, 2002–2003*, p. 26.

7 Auditor-General, *Audit Report No. 18, 2002–2003*, p. 27.

8 Mr Michael Culhane, *Transcript*, 30 April 2003, pp. 4–5.

9 Auditor-General, *Audit Report No. 18, 2002–2003*, p. 34.

10 Mr John Hawley, *Transcript*, 30 April 2003, p. 21.

11 Auditor-General, *Audit Report No. 18, 2002–2003*, Recommendation 1, p. 34.

Finance would also be issuing guidance on special public money¹² and trust money which would focus on the issues of 'classification, management and ongoing good practice.'¹³

Reporting of trust monies

- 5.19 A consequence of misclassifying trust monies is that they may be incorrectly reported in the financial statements of Commonwealth entities. Legal trusts are reported in notes to the entity's financial statements whereas other special accounts are reported in the body of the financial statements.¹⁴
- 5.20 The audit had found that 13 accounts that had been included as trusts in the notes to the financial statements had not been trusts in the legal sense. Consequently, they should have been disclosed in the body of the financial statements.¹⁵
- 5.21 The Committee explored the accounting implications of such misdisclosure.
- 5.22 The ANAO advised the Committee that in the instances identified by the audit, the effect of not accounting for the accounts in the body of the financial statements was not material.¹⁶ Indeed, Defence told the Committee that in its case the misclassification involved an amount of just \$18 000.¹⁷
- 5.23 The ANAO expected that if individual agencies discovered that the effect of misclassification was material they would reclassify their accounts. However, under current accounting standards the reclassification would be for future accounts rather than re-issuing previous accounts. The ANAO added that it had not established whether the misclassification would have a material effect for the whole of the Commonwealth, but no entity's accounts had been qualified because of such a misclassification.¹⁸

Reporting of special public monies

12 Special public money is money held by the Commonwealth, but is not on account of the Commonwealth, or for the benefit or use of the Commonwealth. Trust money is a special category of special public money. Mr Michael Culhane, *Transcript*, p. 5.

13 Mr Michael Culhane, *Transcript*, 30 April 2003, pp. 13–14.

14 Mr Trevor Burgess, *Transcript*, 30 April 2003, p. 8.

15 Mr Trevor Burgess, *Transcript*, 30 April 2003, p. 8.

16 Mr Trevor Burgess, *Transcript*, 30 April 2003, p. 10.

17 Mr Lloyd Bennett, *Transcript*, 30 April 2003, p. 16.

18 Mr Trevor Burgess, *Transcript*, 30 April 2003, p. 11.

- 5.24 The Committee noted the statement in the audit report that ‘the Commonwealth reported almost \$500 million as being held in trust as at 30 June 2001’,¹⁹ and compared this with a figure of \$170 million in the consolidated financial statements (CFS).²⁰
- 5.25 Finance explained that the amount in the CFS reflected special public monies held outside the official public account by FMA Act and CAC Act entities, and did not include special public monies held inside the official public account.²¹ Finance added that it was not true to say that the \$170 million was a component of the \$500 million because ‘the bases upon which [the] two numbers were calculated are fundamentally different.’²²
- 5.26 Finance noted that a written explanation had been provided to the Senate Finance and Public Administration Legislation Committee (SFPALC).²³

Committee comment

- 5.27 The Committee supports the ANAO’s recommendation that agencies review the legal status of the special accounts they had identified as trusts and amend their accounting for them if appropriate.
- 5.28 In the unlikely event that misclassification has a material effect, the Committee does not believe entities should retrospectively alter their financial statements. Instead, in the next set of financial statements there should be a clear indication:
- that the misclassification had occurred; and
 - the effect the misclassification had had on the statements of the previous year.
- 5.29 Regarding the amounts of special public money reported in the audit report and CFS, the Committee is satisfied by the answer provided by Finance at the public hearing, and to the SFPALC. The Committee notes that the CFS is audited by the ANAO and the 2000–01 statements were not qualified in relation to this issue.²⁴
- 5.30 During its review of the Draft Financial Legislation Amendment Bill, the Committee considered at length the nature, establishment and use of

19 Auditor-General, *Audit Report No. 18, 2002–2003*, p. 9.

20 *Transcript*, 30 April 2003, p. 19.

21 Mr Jonathan Hutson, *Transcript*, 30 April 2003, p. 19.

22 Mr Jonathan Hutson, *Transcript*, 30 April 2003, p. 20.

23 Mr Jonathan Hutson, *Transcript*, 30 April 2003, p. 19.

24 Auditor-General, *Audit Report No. 29, 2001–2002, Audits of the Financial Statements of Commonwealth Entities for the Period Ended 30 June 2001*, pp. 37–9.

special accounts. Committee comments on these issues can be found in Chapter 4 of *Report 395*.²⁵

Comcare's compensation payments to agencies

Introduction

- 5.31 The *Safety, Rehabilitation and Compensation Act 1998* (SRC Act) requires Comcare to make all compensation payments directly to Commonwealth employees. Salary payments to employees while a compensation claim is being assessed are considered as advance salary payments which are repayable to the Commonwealth if the claim is successful. The SRC Act prohibits amounts repayable by employees from being automatically offset by payments from Comcare.
- 5.32 The audit found that some agencies had developed less onerous processes. Incapacitated employees continued to receive salary through normal payroll mechanisms while the claim was being assessed, and continued with this payment method if the claim was successful. Comcare paid the organisations—not the employee—in effect reimbursing the organisations for salary payments already made.
- 5.33 The audit report noted advice from the Australian Government Solicitor that compensation monies from Comcare paid to the organisations became special public monies held on behalf of the employee. In these instances the organisation had to obtain the consent of the employee for the compensation monies to be used to offset the salary payments. The audit found that most organisations audited did not treat the Comcare receipts as special public monies, but instead as departmental funds.²⁶
- 5.34 The ANAO recommended that Comcare review the administration of compensation payments under the SRC Act to 'ensure that the process represents the efficient, effective and ethical use of Commonwealth resources while protecting the rights and entitlements of individuals concerned.' The audit report added that sections of the SRC Act prescribing the administrative arrangements for compensation monies should be assessed for their appropriateness.²⁷

25 JCPAA, *Report 395, Review of the draft Financial Framework Legislation Amendment Bill*, Canberra June 2003, Chapter 4, pp. 25–50.

26 Auditor-General, *Audit Report No. 18, 2002–2003*, pp. 36–7.

27 Auditor-General, *Audit Report No. 18, 2002–2003*, Recommendation 2, p. 38.

- 5.35 Comcare agreed with the recommendation and responded that ‘because amendment of the SRC Act will be required, the current arrangements may continue for some time.’²⁸

Committee comment

- 5.36 The Committee considers that Comcare’s procedures regarding compensation payments to incapacitated employees are efficient and effective—a view supported by comments in the audit report. Unfortunately, these procedures do not conform to the requirements of the SRC Act.
- 5.37 At the time of the public hearing, the Committee was reviewing the draft Financial Framework Legislative Amendment Bill (FFLAB) and suggested to Finance witnesses that the FFLAB be used to amend the SRC Act.²⁹ In a subsequent submission to the Committee’s review of the FFLAB, Finance advised that it will propose that amendments to the SRC Act be included in the FFLAB.³⁰

28 Auditor-General, *Audit Report No. 18, 2002–2003*, p. 38.

29 *Transcript*, 30 April 2003, p. 4.

30 JCPAA, *Report 395*, p. 57, referring to Finance, *Submission No. 17*, pp. 48–9.

Audit Report No. 19, 2002–2003

The Australian Taxation Office's Management of its Relationship with Tax Practitioners

Introduction

Background

- 6.1 Tax practitioners assist taxpayers to deal with their taxation responsibilities and have become an integral part of the tax system. Although tax practitioners are a wide group of professionals working on taxation matters, the audit focused on the Australian Taxation Office's (ATO's) management of its relationships with tax agents. This was because tax agents form the core of the tax practitioner group and have a fundamental role in the effective operation of the tax system.
- 6.2 Despite the diversity in their activities and relationships with their clients, tax practitioners have an important role because they interpret the law, advise taxpayers and 'educate' taxpayers in tax law matters and in some

cases submit information to the ATO on behalf of their clients (i.e. taxpayer information).

6.3 The significance of tax practitioners in the operation of the tax system has increased markedly in recent decades because of:

- the rapid expansion of the scope and complexity of tax law, accompanied by shifts in reporting obligations on taxpayers flowing from the New Tax System;
- the growth in complexity of business operations in the economy;
- more involvement of individual taxpayers in investment activities and income sources other than personal exertion;
- increased use of the tax system to make social payments as well as to collect revenue; and
- the shift towards self-assessment as the guiding principle of tax administration.

6.4 The audit noted that the ATO had formally recognised that tax practitioners were critical to the efficient and effective operation of the tax system because:

- they streamlined the processes and linkages between the ATO and taxpayers; and
- they were able to influence their clients' behaviour, thereby providing a key means to secure taxpayer compliance.

6.5 Tax practitioners can also benefit from their participation as ATO–taxpayer intermediaries because:

- they could access the ATO's support services—priority services in some instances; and
- they could enter the regulated tax agent segment of the profession.

6.6 The audit also noted ATO's stated position that, as a priority, it invested in strategies to support the interaction of tax agents with the tax system. This was because tax agents perform significant processing functions and because they were critical for the ATO's education and communication efforts.¹

1 Auditor-General, *Audit Report No. 19, 2002–2003, The Australian Taxation Office's Management of its Relationship with Tax Practitioners*, Canberra, December 2002, pp. 11–13.

The tax practitioner population

- 6.7 The number of tax practitioners is understood to be increasing in Australia. However, apart from tax agents—a group which is regulated, the ATO does not have comprehensive data on the total number or characteristics of the tax practitioner population. This is because the ATO is often unaware of the tax practitioner's interaction with taxpayers as it may not involve the ATO at all. However, these interactions (e.g. the tax advice the tax practitioner provides) may affect the ATO's administration of the tax system.
- 6.8 However, the ATO does have information on tax agents who form the largest component of the tax practitioner population. Approximately 25 000 tax agents were registered in 2001–02. Registration is undertaken under by independent statutory bodies, the Tax Agents' Boards (TABs), in each State.
- 6.9 The tax agent population has the following broad characteristics:
- each tax agent has, on average, 599 clients, but around half have fewer than 100 clients;
 - close to 50 per cent of practices are located in inner metropolitan areas; and
 - 80 per cent of the tax agent client base are individual taxpayers.
- 6.10 The use by taxpayers of registered tax agents has grown over time. In 1980, approximately 20 per cent of individual taxpayers sought professional assistance from tax agents to prepare income tax returns. By 2001, the proportion had risen to 76 per cent. The significance of tax agents' involvement in the tax system is shown by ATO processing statistics—in 2001–02, tax agents accounted for:
- 76 per cent of the 10.1 million individual returns;
 - 94 per cent of the 0.6 million company returns; and
 - 51 per cent of the 1.8 million quarterly Business Activity Statements (BASs).²

The Australian Taxation Office's relationship with tax practitioners

- 6.11 In its dealings with tax practitioners, the ATO has to balance often divergent interests in an environment where issues are sometimes not
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2 Auditor-General, *Audit Report No. 19, 2002–2003*, pp. 13–14.

under the control of either party. Tax practitioners can also interact with many different areas of the ATO. The different legislated functions of the ATO determine a range of different types of interaction, including:

- client support—providing legislation, policy and system advice;
- service support—providing information, technical and procedural assistance;
- active compliance; and
- regulatory support.³

Management structure and resourcing

6.12 All of the ATO's business and service lines interact from time to time with the various categories of tax practitioners. However, a unit has been established within ATO's Personal Tax business line to specifically manage and coordinate relationships with tax agents. The unit is titled the Tax Practitioner Group and Alliances Branch (TPG&A).

6.13 The ATO also consults and interacts with the other categories of tax practitioners as they are stakeholders who may represent or influence taxpayers. The major interactions are by way of:

- the ATO consultative bodies representing the personal tax, small business and large business sectors;
- key client manager relationships with large business participants in the financial advisory sector; and
- consultations with tax agents and professional associations with interest in GST issues.⁴

6.14 The ATO does not collect and attribute the costs of its management of relations with tax practitioners, or the tax agent segment, because costs are diffused throughout the ATO's business lines. However, for 2001–02 the TPG&A's direct costs were \$11.7million. As well, in 2001–02 the cost of the ATO Business Call Centre—the call centre most heavily used by tax practitioners—was \$56.4 million.⁵

3 Auditor-General, *Audit Report No. 19, 2002–2003*, pp. 14–15.

4 Auditor-General, *Audit Report No. 19, 2002–2003*, p. 15.

5 Auditor-General, *Audit Report No. 19, 2002–2003*, p. 15.

The audit

- 6.15 The audit focused on the various ATO–tax practitioners relationships which broadly matched the major functional areas of the TPG&A. Particular relationships reviewed were:
- ATO's regulatory relationship with tax agents;
 - the service support relationship with tax agents;
 - ATO's relationship with tax agents and members of the wider tax practitioner group in the professional bodies; and
 - ATO's call centre service support relevant to tax agents.
- 6.16 The audit took into account recent changes in the ATO's activities arising from an agreement between the ATO and the tax and accounting professional bodies in September 2002. The agreement was to improve ATO services with the initial priorities to include:
- the appointment of an ATO senior executive to coordinate support programs for tax agents, reporting directly to the Commissioner;
 - the development of 'client' relationship manager models;
 - improvement to on-line and telephone services; and
 - enhanced transparency of performance statistics and information relating to tax agents.⁶
- 6.17 The audit did not examine the ATO's provision of client support by way of ATO systems and legislation, or the compliance activities administered by areas of the ATO other than TPG&A.

Audit findings

- 6.18 The audit acknowledged that ATO's management of its relationship with tax practitioners was a challenging task. Interactions were dynamic, multi-dimensional and necessarily involved ambiguity and the balancing of different interests. The relationship was also affected by factors, ranging from small, operational matters, to high-level strategic issues and matters outside the control of the parties themselves. A further complicating factor was that tax practitioners were a heterogeneous group.

⁶ Auditor-General, *Audit Report No. 19, 2002–2003*, p. 16.

- 6.19 The current relationship could generally be described as strained and tense. Consultations showed that the ATO and tax agents and some other tax practitioners perceived a considerable measure of dissatisfaction with the relationship. Further, on a range of measures, overall perceptions of the relationship had been negative, and increasingly so, in some areas. It was considered that the situation had arisen largely due to the pressures placed of tax reform on tax agents, other tax practitioners, and on the ATO's operational systems.
- 6.20 The ATO recognised that improvements were required particularly with in its relationship with tax agents. Initiatives aimed at better managing and enhancing the relationship have included:
- dedicated phone services and special complaint resolution services;
 - more extensive consultation processes with tax agents, and members of tax and accounting professional bodies; and
 - reactivation of consideration of reform in the regulation of tax agents.
- 6.21 The ANAO noted that useful mechanisms had been established to support tax agent relationship management, and this was accompanied by a renewed commitment from senior ATO staff.
- 6.22 To manage its complex relationship with tax agents, the ATO had established appropriate internal management, oversight and coordination mechanisms across its business lines. It also maintained a range of external liaison, consultation and communications systems that enabled two-way dialogue with representatives of tax agents and the tax and accounting professional bodies. While the ATO had substantial information about the characteristics of tax agents, its knowledge of characteristics highlighting possible risks of non-compliance was less comprehensive. Rectifying this knowledge gap was important because tax agents' fundamental importance to the tax system.
- 6.23 Although the ATO had a statement of principles on tax agent relationship management, there needed to be an integrated and consistent statement of its intended strategic relationship with tax agents which acknowledged the many dimensions of the ATO/tax agent relationship.
- 6.24 Regarding the wider tax practitioner group, the ATO's separate strategies were based on tax practitioner risk and influence in the tax system. A strategic framework for its relationship would be enhanced by the ATO ensuring its strategies specify the objectives of its interactions and how these objectives would be pursued.

- 6.25 The ATO had not developed performance information for the relationship management systems for tax agents and the members of tax and accounting professional bodies with which the ATO formally consulted. There also was no clear, comprehensive or consistent statement of the respective roles and responsibilities of itself and tax agents in the operation of the tax system.
- 6.26 The ATO was properly emphasising its tax agent compliance responsibilities in its regulatory relationship with tax agents. A differentiated service approach was being developed to secure taxpayer compliance through tax agents and other tax practitioners, such as the providers of BAS services. This was based on modelling performance characteristics of tax agents and tax practitioners in question, and using combined incentives and penalties. A range of education, information and call centre services had also been established over the years to assist tax agents fulfil their role.
- 6.27 However the lack of a consistent strategic framework for ATO's relationship with tax agents constrained the ATO's ability to maximise the benefits of its relationships from both an administrative efficiency and compliance viewpoint.
- 6.28 The National Review of Standards for the Tax Profession in 1994 noted the challenges and ideas for reform of the tax agent regulatory framework. However, the fundamental reform canvassed in that report has yet to occur. From July 2002, responsibility for the design of tax law and regulations, including for the review of standards for the tax profession, was passed from the ATO to the Treasury. The ATO no longer contributes to policy development and design but will continue to provide advice on administrative impacts. Resolving this longstanding matter of reforming the regulatory framework may assist the ATO's relationship with tax agents.⁷
- 6.29 The Auditor-General made ten recommendations to which the audited agencies agreed, or agreed in principle.⁸

The Committee's review

- 6.30 Two agencies were invited to give evidence to the Committee at a public hearing on Wednesday, 30 April 2003. The agencies were:

7 Auditor-General, *Audit Report No. 19, 2002–2003*, pp. 16–19.

8 Auditor-General, *Audit Report No. 19, 2002–2003*, pp. 30–3.

- the Australian National Audit Office; and
- the Australian Taxation Office.

6.31 The Committee took evidence on the following issues:

- tensions between the ATO and tax practitioners;
- the tax agent profile;
- tax agent competency;
- consultation processes with tax agents; and
- communication systems available to tax agents.

Tensions between the Australian Taxation Office and tax practitioners

6.32 The ATO noted that Australia was unusual in there being a close relationship between the ATO and tax practitioners.⁹ There would always be a tension in the relationship because the ATO was the law interpreter and the checker of compliance. The aim was to make the natural tension a positive and professional tension.¹⁰

6.33 However, the introduction of new tax system had caused additional pressures and the time of audit fieldwork 'was a very tense period'.¹¹

6.34 The Committee acknowledges that the introduction of taxation reforms was a time of change and learning for both the ATO and tax practitioners. The Committee is pleased with the advice from the ATO that it monitors its relations with its stakeholders,¹² and with the advice that at the time of the public hearing the relationship with the Institute of Chartered Accountants of Australia had improved.¹³

Tax agent profile

6.35 Evidence provided by the ATO indicated that tax agents play a pivotal role in the lodgement of income tax returns. Tax agents lodged about 98 per cent of business, and about 75 per cent of individual non-business, tax returns.¹⁴

9 Mr Mark Konza, *Transcript*, 30 April 2003, p. 25.

10 Ms Jennifer Granger, *Transcript*, 30 April 2003, p. 26.

11 Ms Jennifer Granger, *Transcript*, 30 April 2003, pp. 25–6.

12 Ms Jennifer Granger, *Transcript*, 30 April 2003, p. 25.

13 Mr Steve Chapman, *Transcript*, 30 April 2003, p. 37.

14 Ms Jennifer Granger, *Transcript*, 30 April 2003, p. 36.

- 6.36 The ATO provided an update to the Committee of its response to the ANAO's recommendation which was in part 'to identify and analyse the characteristics of the tax agent population.'¹⁵
- 6.37 The ATO told the Committee that it was embarking on research with the professional associations entitled 'The World of the Tax Agent'. The research had provided information on:
- the demographics of tax agents;
 - indicators of tax agent business success; and
 - the factors which motivate and frustrate tax agents.
- 6.38 The average age of tax agents was reflective of the 'baby boomer' profile of Australia. This meant that over the next few years significant numbers of tax agents would be retiring and would need to be replaced. Unfortunately, research showed that younger graduates were not looking to public practices for their career. The ATO was working with the accounting profession to address this likely shortfall.¹⁶
- 6.39 The ATO told the Committee that indicators of tax agent business success concerned their business practices such as:
- how they structure the operations of their firm;
 - the strong correlation between the profitability of a practice and the success of the practice; and
 - the take-up and use of technology, with computerisation and online accessing of the ATO.¹⁷
- 6.40 The ATO's research indicated that broad compliance work was the main task of tax agents. Many obtained personal fulfilment from their role facilitating their client's success. The witness added:
- One of the frustrations they are seeing at the moment is that too much of their time is being spent on regulatory tort work when they would like to spend more time on business planning and giving business advice to their client. That suggests the need to improve the level of technology, streamline operations or even improve the levels of service we provide.¹⁸

15 Auditor-General, *Audit Report No. 19, 2002–2003*, Recommendation 5, p. 79.

16 Mr Steve Chapman, *Transcript*, 30 April 2003, pp. 29–30.

17 Mr Steve Chapman, *Transcript*, 30 April 2003, p. 30.

18 Mr Steve Chapman, *Transcript*, 30 April 2003, p. 30.

- 6.41 The Committee believes that information on the tax agent population provides a valuable tool to the ATO. While the Committee notes ATO advice that the compliance profile of tax agents is part of future phases of the research,¹⁹ this important aspect of profiling should not be overlooked.

Tax agent competency

- 6.42 The Committee asked the ATO whether it had considered evaluating the quality of tax agent services through ATO staff posing as clients and seeking taxation advice.
- 6.43 The ATO responded that it did not engage in this form of consumer protection. The witness added that most tax agents belonged to a professional body and were bound by the code of conduct and ethical arrangements of those bodies. Another quality control mechanism was for tax agents considered to be deficient to be referred to the appropriate state taxation board.²⁰
- 6.44 The ATO was unaware of state taxation boards undertaking covert assessment of tax agents. The boards would tend to 'get a good feel for how an agent is operating' from the number of complaints about a particular agent. However, the boards did not operate like a department of fair trading and an agent would 'have to stuff up pretty badly to really warrant any sort of stern action from a tax agents board.' Generally complaints from the public would be lodged with a state department of fair trading.²¹
- 6.45 In dealing with tax agent competency, the ATO told the Committee that it preferred an educative approach. If a tax agent was found to be systematically claiming incorrect amounts or applying the law incorrectly, the ATO would discuss the issue with the agent. In extreme cases it was open for the ATO to refer the issue to a taxation board.²² Following the hearing the ATO advised the Committee in a supplementary submission that it had referred 33 cases to the state tax agents boards in the previous year.²³
- 6.46 The ATO's submission also noted that tax agents were subject to a three years registration cycle with state taxation boards and that tax agents were

19 Mr Steve Chapman, *Transcript*, 30 April 2003, p. 30.

20 Mr Steve Chapman, *Transcript*, 30 April 2003, pp. 33–4.

21 Mr Mark Konza, *Transcript*, 30 April 2003, p. 34.

22 Mr Steve Chapman, *Transcript*, 30 April 2003, p. 34.

23 ATO, *Submission No. 19*, p. 3.

sometimes deregistered. For example in the financial year 2002–03, tax agents boards had:

- received 563 written complaints;
- cancelled 86 registrations;
- written to 199 tax agents asking them to show cause;
- referred 94 tax agents to the Tax Office for investigation; and
- suspended 5 tax agents.²⁴

6.47 Regarding the promoters of taxation schemes, the Committee was advised the ATO had a promoters task force. The aim of the task force was to identify at an early stage taxation arrangements which raised ATO concern. The ATO was prepared to issue alerts to advise tax agents of its concern about particular schemes and that it was investigating particular promoters.²⁵

Consultation processes with tax agents

6.48 The Committee drew attention to the demands placed on tax agents when they contributed to ATO consultative committees and raised the issue of whether they should be remunerated for their efforts.

6.49 The ATO responded that when it talked to tax agents it always asked them if they wished to become a member of one of the consultative committees. Tax agents were never pressured to contribute and the ATO was 'very conscious of getting a wide range and a base so that we get a representative sample of agents.'²⁶

6.50 The ATO added that recently it had worked with particular tax agents to allow them to contribute at a level which was more manageable for them. This involved finding more representative agents and working with agents to 'bring forward people in their networks, people they [could] trust as good representatives.'²⁷

6.51 The ATO told the Committee that it considered remuneration when it was accessing particular expertise, but:

24 ATO, *Submission No. 19*, p. 1.

25 Ms Jennifer Granger, *Transcript*, 30 April 2003, p. 35.

26 Mr David Diment, *Transcript*, 30 April 2003, p. 32.

27 Mr Mark Konza, *Transcript*, 30 April 2003, p. 33.

... where we are consulting more because of an agent's ability to represent their client's experience and represent the experiences of their peers and so forth, we do not generally remunerate ...²⁸

- 6.52 The Committee does not consider it appropriate for the ATO to remunerate tax agents who are members of consultative committees. Membership of a consultative committee brings benefits other than financial, such as credibility with peers, and first hand knowledge of ATO position on issues and initiatives. Moreover, for remuneration to be more than token, it would have to be reasonable—such a level of remuneration could distort the sample of tax agents serving on consultative committees and make it unrepresentative.

Communication systems available to tax agents

Telephone systems

- 6.53 The ATO advised the Committee that a free call 1300 telephone number was now available to callers requiring information on tax matters. The system allowed calls to be redirected to the relevant ATO officer, even to mobile phone numbers, without incurring a charge to the caller.²⁹
- 6.54 Further, a survey had indicated that improvements in the telephone system had made available to accountants the equivalent of an additional four hours a week for other work.³⁰ The ATO was able to analyse the 60–65 thousand calls it received each week and had discovered that some tax agents made multiple calls. This was often because they did not know where they could access the information themselves.³¹
- 6.55 Identification of such problems had led to the development of the ATO's internet tax agent portal.

Tax agent portal

- 6.56 The ATO's tax agent portal is designed to enable tax agents to obtain information concerning their clients, including:
- client lists of those who had or had not lodged a return;
 - real time on-line access to their client's accounts to view debts, their make up and transaction history;

28 Mr Mark Konza, *Transcript*, 30 April 2003, p. 33.

29 Mr Steve Chapman, *Transcript*, 30 April 2003, p. 27.

30 Mr Steve Chapman, *Transcript*, 30 April 2003, p. 30.

31 Ms Jennifer Granger, *Transcript*, 30 April 2003, p. 31.

- a secure message service unlike the normal email service;
- the ability in the future to request funds or the transfer of funds between particular accounts; and
- the ability to update addresses on the ATO's business register.³²

6.57 The ATO advised that the current security was at the SSL level 128-bit security with a password and a personal identification number. It was hoped to move towards the use of the public-private key infrastructure.³³

Committee comment

- 6.58 The Committee endorses the ATO's endeavour to improve its communication with tax agents. The Committee expects that the ATO tax agent portal to be continually reviewed to take advantage of advances in information technology.
- 6.59 Notwithstanding the improvements to the ATO's communication with tax agents, the Committee is concerned with the cost of compliance with the taxation system.

32 Mr Steve Chapman, *Transcript*, 30 April 2003, p. 32.

33 Mr Steve Chapman, *Transcript*, 30 April 2003, p. 32.

Audit Report No. 25, 2002–2003

Financial Statements of Commonwealth Entities for 2001–02

Introduction

Background

- 7.1 The *Financial Management and Accountability Act 1997* (FMA Act) and the *Commonwealth Authorities and Companies Act 1997* (CAC Act), require the Auditor-General to report each year on whether the financial statements of Commonwealth entities have been prepared in accordance with the Finance Minister's Orders, and whether they give a true and fair view of the matters required by those orders.¹
- 7.2 The ANAO is responsible for the audit of the financial statements of 257 Commonwealth entities. These include:
- 82 agencies;

1 Section 57 of the FMA Act sets out the requirements for agencies and clause 3, part 2 of Schedule 1 of the CAC Act sets out the requirements for other Commonwealth bodies.

- 117 Commonwealth authorities and their subsidiaries; and
 - 42 Commonwealth companies and their subsidiaries.²
- 7.3 The material portion of the Commonwealth's revenues, expenses, assets and liabilities in the 2001–2002 financial year are accounted for by a relatively small number of Commonwealth entities, notably:
- the Department of Defence (Defence);
 - the Department of Family and Community Services;
 - the Department of Health and Ageing; and
 - the Australian Taxation Office (ATO).³

The audit

- 7.4 The audit focused on the final results of the financial statement audits for 2001–2002. These included the Consolidated Financial Statements (CFS) and the financial statements of Commonwealth entities. The audit report also included comments on financial management issues arising from the audits, in particular their relation to internal control structures.

Audit findings

- 7.5 The significant findings and comments in the audit report were:
- comments on the harmonisation of standards used to prepare the Commonwealth's two key financial reports—the CFS and the Final Budget Outcome (FBO);
 - comments on the timeliness of the preparation of entity financial statements;
 - audit qualifications of the CFS concerning:
 - ⇒ the estimation of taxation revenue by the taxation liability method (TLM) which did not conform to AAS 31 *Financial Reporting by Governments*;
 - ⇒ the accounting treatment of the collection of the Goods and Services Tax (GST);

2 Auditor-General, *Audit Report No. 25, 2002–2003, Financial Statement Audit, Audits of the Financial Statements of Commonwealth Entities for the Period Ended 30 June 2002*, Canberra, December 2002, p. 12.

3 Auditor-General, *Audit Report No. 25, 2002–2003*, p. 12.

- ⇒ insufficient audit evidence to support the figure for Defence's inventory and repairable items under the Specialist Military Equipment balance;
- an 'emphasis of matter'⁴ in relation to the CFS because of inherent uncertainty about the potential Commonwealth liabilities arising from both the HIH Insurance Group collapse and the indemnity provided to the provisional liquidator of United Medical Protection Ltd and Australasian Medical Insurance Ltd (UMP/AMIL);^{5,6} and
- four financial statements which were qualified:
 - ⇒ the CFS, for differences in accounting policies and limitations in scope (referred to above);
 - ⇒ the ATO, for a disagreement in the accounting treatment of its lease of IT equipment;
 - ⇒ Defence, concerning its inventory and specialist military equipment repairable items (referred to above); and
 - ⇒ the National Gallery of Australia, because its reliance on fund raising through public donations could not assure the completeness of its revenue.⁷

The Committee's review

7.6 Four agencies were invited to give evidence to the Committee at a public hearing on Wednesday, 30 April 2003. The agencies were:

- the ANAO;
- the ATO;
- Defence; and
- the Department of Finance and Administration (Finance).

7.7 The Committee took evidence on the following issues:

4 An emphasis of matter is not an audit qualification. It can arise because of inherent uncertainty in the figures reported in a statement; when information in the document containing the financial statement is inconsistent with that in the financial report; and when it is highly unlikely the entity will continue as a going concern because of information arising after reporting and there has been adequate disclosure in the financial statements.

5 The CFS had recognised a Commonwealth liability of \$496 million for the HIH collapse and \$500.8 million for the UMP/AMIL liquidator. Both were based on actuarial assessment, but the final amounts were uncertain. This was noted on the audit of the CFS as an 'emphasis of matter'.

6 Auditor-General, *Audit Report No. 25, 2002–2003*, p. 31.

7 Auditor-General, *Audit Report No. 25, 2002–2003*, pp. 36–7.

- harmonisation of Australian and international accounting standards;
- auditing of the FBO;
- timeliness in the preparation of Commonwealth entity financial statements;
- qualification of Defence's financial statement;
- use of the TLM for estimating taxation revenue;
- accounting treatment of GST revenue; and
- accounting treatment for the lease of ATO's information technology equipment.

Harmonisation of accounting standards

- 7.8 The Commonwealth's two key financial reports—the CFS and the FBO—are prepared using two different external reporting standards. The two standards are Australian Accounting Standard 31, *Financial Reporting by Governments* (AAS31) and the Government Finance Statistics (GFS).
- 7.9 AAS31 comprises a set of rules concerned with measuring economic transactions and events, and presenting those measurements in a manner that conveys financial performance, financial position, cash flows and other relevant disclosures. The aim is to provide users with relevant information to enable resource allocation decisions and to report on stewardship.
- 7.10 The GFS framework was developed by the International Monetary Fund in co-operation with the World Bank, Eurostat and the Organisation for Economic Co-operation and Development (OECD). The aim of the GFS is to measure the impact of public policy, including the measurement of a government's contribution to the economy. It facilitates public sector input into the preparation of national accounts.⁸
- 7.11 The CFS is prepared under AAS31, is audited and is tabled in Parliament some time after the end of each financial year.⁹ On the other hand, the FBO contains some information prepared under AAS31 and other information prepared under GFS. The FBO contains audited information (that prepared under AAS31) and unaudited information, and is required under the *Charter of Budget Honesty Act 1998* to be tabled by 30 September each year.

8 Finance, *Briefing Paper to the JCPAA*, 17 June 2003.

9 For the 2001–02 Financial Year the CFS was tabled on 29 November 2002.

7.12 The audit report commented:

The two frameworks often result in confusion and difficulties in interpreting information. While a considerable amount has been done to harmonise the reporting frameworks, significant differences remain, including in respect of the treatment of:

- revaluation of assets;
- foreign exchange gains and losses;
- interest flows related to swaps and other financial derivatives; and
- acquisitions of defence weapons platforms.¹⁰

7.13 The ANAO supported the harmonisation of reporting standards. It noted that while it was primarily a matter for the Australian Accounting Standards Board, support from stakeholders involved in public sector accounting would be needed, especially in the light of Australia's commitment to adopt international accounting standards by 2005.¹¹ (A briefing paper prepared for the Committee by Finance noted that the harmonised standard is to take effect by 1 July 2004.)

7.14 Finance told the Committee that the OECD had a keen interest in creating a single reporting framework and had recently examined the treatment of defence weapons platforms. The Australian Accounting Standards Board had also started reviewing a draft strategic plan to deal with harmonisation, which called for the Board to review draft standards in early 2004.¹²

Auditing the Final Budget Outcome

7.15 Division 3, Schedule 1 of the *Charter of Budget Honesty Act 1998* requires the Treasurer to publicly release and table the FBO no later than 3 months after the end of the financial year.

7.16 The Final Budget Outcome comprises four parts:

- Part 1: Budget aggregates (revenue, expenses, net capital investment, cash flows, net debt and net worth) for the general government sector;¹³
- Part II: Commonwealth financial statements (operating statement, balance sheet, cash flow statement) for the general government sector, public non financial corporations and public financial corporations;¹⁴

10 Auditor-General, *Audit Report No. 25, 2002–2003*, p. 18.

11 Auditor-General, *Audit Report No. 25, 2002–2003*, p. 19.

12 Mr Brett Kaufmann, *Transcript*, 30 April 2003, pp. 62–3.

13 Principally entities bound by the FMA Act.

- Part III: Primary financial statements for the general government sector; and
- Part IV: payments to local governments, states and territories (GST revenue, general revenue assistance, general purpose assistance to local government, and specific purpose payments to the states and territories).

7.17 The FBO has not been audited.¹⁵

7.18 In *Report 388, Review of the Accrual Budget Documentation*, tabled in June 2002, the Committee recommended that the FBO should be audited by the ANAO.¹⁶

7.19 The ANAO response to the recommendation agreed that an audit would provide additional assurance to users of the FBO, but added that this initiative would have resource implications for the ANAO and that it was a matter for the Government and the Parliament to decide.¹⁷

7.20 The Government did not agree to the Committee's recommendation. The Government response to the recommendation stated:

The Government notes that the Final Budget Outcome must be published by 30 September, in accordance with the *Charter of Budget Honesty Act 1998*. Under present arrangements this deadline is met with little time to spare. Therefore, the introduction of a complete audit process would compromise this legislative requirement. As the individual agency accounts that are consolidated into the FBO are audited, there is already an implicit audit process undertaken.

The Consolidated Financial Statements (CFS) for the Commonwealth are already audited by the Australian National Audit Office. Under the *Financial Management and Accountability Act 1997* the CFS must be tabled within five months of the end of the financial year. Given that audit of the CFS already provides assurance on aggregate financial statements, the Government does

14 Bodies covered by the FMA Act and entities bound by the CAC Act, such as the Reserve Bank of Australia and other borrowing authorities.

15 However, before the adoption of the accrual accounting framework by the Commonwealth, the Finance Minister's Aggregate Financial Statement (AFS) contained a section called the 'Budget Outcome'. This section was expressed in a cash accounting terms and contained some, but not all, of the information that is now contained in the FBO. The AFS was audited.

16 JCPAA, *Report 388, Review of the Accrual Budget Documentation*, Canberra, June 2002, Recommendation 11, p. 81.

17 Auditor-General, *Response to Report 388*, 6 September 2002, p. 3.

not consider it necessary to add another layer of checking for the FBO with associated consequences for what is already a tight FBO timetable.¹⁸

7.21 The ANAO provided further advice regarding the potential audit of the FBO in the audit report:

The issue of relevant standards to be used would be central to such an audit.

An audit of the FBO Report would, in the first instance, entail a review of the general government sector component of the CFS, to ensure consistency of input to, and presentation of, the FBO Report. Secondly, a component of such an audit would include a review of the Commonwealth financial statements to determine adherence with the relevant GFS framework.¹⁹

Timeliness of preparing financial statements

7.22 In auditing the 2001–02 financial statements of Commonwealth entities, the ANAO noted that there had been a deterioration in timeliness when compared to the statements of the previous year:

- the first draft financial statements for presentation to the ANAO took 45 days in 2001–02, an increase of 19 days;
- signed financial statements were produced after 65 days, an increase of 5 days; and
- financial statements were tabled in Parliament 116 days after the end of the financial year, an increase of 6 days.²⁰

7.23 The ANAO suggested that the decline in timeliness was due to the restructuring of a number of agencies following the Administrative Arrangements Order of 26 November 2001 and changes to financial reporting requirements outlined in the 2002 Finance Minister's Orders.

7.24 Nevertheless, the recommendations of the Finance Budget Estimates and Framework Review required a progressive improvement in the timeliness of reporting accrual budget outcomes. As a result, for the 2004–05 financial

18 Senator the Hon Nick Minchin, Minister for Finance and Administration, *Government Response to Report 388*, 2 May 2003, p. 4.

19 Auditor-General, *Audit Report No. 25, 2002–2003*, p. 19.

20 Auditor-General, *Audit Report No. 25, 2002–2003*, p. 21.

year, entities would have to ‘improve the timeliness of their financial reporting by, on average, at least 25 days.’²¹

7.25 To meet this target entities would have to re-engineer and upgrade processes focussing on speed of processing and reporting, while also improving data integrity and financial analysis. There was also the need to produce quality monthly financial reports with supporting analysis and involve the senior executive group in the process.²²

7.26 The Committee explored with witnesses the challenges facing agencies in the timely presentation of financial statements for audit. Defence responded that it had:

... an old system that was not designed for this environment, which forces us to rely on substantive processes, quality assurance processes, and work-around processes to achieve quality in the results.²³

7.27 Whereas Defence was confident it could present ‘signed off reports’ in a more timely manner in 2002–03, the ANAO did not display a similar level of confidence.²⁴

7.28 The ANAO told the Committee that the Department of the Treasury (Treasury) took twice as long to prepare its draft financial statements because of the complexity of bringing to account the figures involved in the HIH Support Scheme and the Medical Assistance Scheme.²⁵ The Committee notes that the level of uncertainty surrounding the figures resulted in a an ‘emphasis of matter’ by the ANAO.

7.29 Finance provided the Committee with further information on timeliness in the following table:

Table 1 Average no. of days to lodge audit cleared financial statements with Finance compared with due date.

Agency	2000–01 actual	Target days	2001–02 actual	Target days	Slippage between years	Slippage from target
Material	47.6	46	48.6	46	1	2.6
Small	68	79	77.4	78	9	0

Source Finance, *Submission No. 14*, p. 4.

21 Auditor-General, *Audit Report No. 25, 2002–2003*, p. 22.

22 Auditor-General, *Audit Report No. 25, 2002–2003*, p. 23.

23 Mr Lloyd Bennett, *Transcript*, 30 April 2003, p. 58.

24 Mr Michael Watson, *Transcript*, 30 April 2003, p. 58.

25 Mr Trevor, *Transcript*, 30 April 2003, p. 59.

- 7.30 Finance advised that smaller agency audits are scheduled to commence after the audits of the material agencies in their portfolio are completed. As well, the introduction of monthly financial reporting for small agencies in 2003–04 ‘should lead to improvements to their financial reporting processes and procedures once it becomes a regular and ongoing activity.’²⁶
- 7.31 In *Report 388*, the Committee recommended that the reporting requirements for agency annual reports should be brought forward by one month to 30 September. While the Government did not agree, it advised that earlier targets for the provision of financial information by agencies had been agreed to. With the implementation of these targets progressively ‘over the next three years’ the Government may then be in a position to reconsider the issue of deadlines for tabling of annual reports.²⁷

Committee comment

- 7.32 The Committee still considers that the FBO should be audited. However, there are two significant impediments to achieving this goal:
- the need to determine which audit standards to use to audit the FBO; and
 - the difficulty of preparing and also auditing the FBO within three months of the end of the financial year.
- 7.33 The Committee supports the efforts of Finance to facilitate the harmonisation of reporting standards, but cautions that harmonisation should not come at the expense of the quality provided by the existing Australian standard. When harmonisation is achieved—and the target is 1 July 2004—the first impediment would largely be overcome.
- 7.34 The Committee is encouraged by the move to progressively bring forward the provision of financial information by agencies. When this is achieved, audited financial statements will be available for incorporation into whole of government reports at an earlier date. Consequently, completion of the FBO could be expected earlier, which would provide more time if it was decided to audit the FBO. Thus the second impediment could largely be overcome through the passage of time.

26 Finance, *Submission No. 14*, p. 4.

27 Senator the Hon Nick Minchin, Minister for Finance and Administration, *Government Response to Report 388*, 2 May 2003, p. 2.

- 7.35 The Committee will continue to have an interest in the initiative of auditing the FBO, but recognises that this goal is achievable only in the medium term.

The qualification of Defence's financial statement

- 7.36 Defence's financial statements were qualified because there was insufficient audit evidence to support the figures for Defence's inventory and the repairable items under the Specialist Military Equipment balance. This qualification flowed through to the CFS because of the materiality of the issue.
- 7.37 The audit opinion resulted from the lack of controls over the Standard Defence Supply System (SDSS) which manages the items. Users of the system were able to enter data directly into the price field without sufficient controls and it was not possible to assess with confidence the cumulative financial effect of prices that had been inadvertently adjusted or incorrectly calculated. The ANAO had also criticised the price integrity of explosive ordnance on the COMSARM logistics system.²⁸
- 7.38 At the hearing the ANAO referred to specific problems identified in the audit report which included:
- more than \$482 million of the \$1 574 million of asset write-downs were generated by the SDSS;
 - \$243 million of the \$694 million worth of assets brought onto the books were generated by the SDSS;
 - prices of explosive ordnance were changed at operational level without documentation and retention of the rationale;
 - where explosive ordnance was purchased under contract with escalation clauses, the system did not record the accurate value;
 - the ANAO did not have confidence as to the existence of all the assets recorded on the SDSS at 'positions' outside Defence warehouses, notwithstanding the 'signing off' by Defence that the processes were robust;
 - some \$187 million worth of Specialist Military Equipment had a fifty per cent chance of not being recorded; and
 - total unrecorded assets could be as high as \$255 million.²⁹

28 Auditor-General, *Audit Report No. 25, 2002–2003*, pp. 30–1.

29 Auditor-General, *Audit Report No. 25, 2002–2003*, p. 87.

- 7.39 Defence assured the Committee that the issue of inventory pricing and repairable items did not impact on Defence's 'capability to perform, nor [did] they reflect any demands on cash or any fraudulent activity.'³⁰
- 7.40 Defence continued by drawing attention to the limitations of its SDSS:
[It was] very much designed on quantity managing an item as opposed to capturing the financial information ... It was developed in the early eighties ... it was put in place before the requirement for accrual accounting came in. So it was never designed as a financial management tool. ... When you issue assets from warehouses to the bases ... that is where the system is weak at the moment. That is because it is allowing people to issue to the base, and the base does not necessarily keep that information up to date on the system. ... We are not confident of the quantities on the system. We are now trying to get people to do the stocktakes on the bases to verify and clean up the numbers.³¹
- 7.41 Regarding the issue of potential fraud, the ANAO advised the Committee that Defence conducted fraud control and statistically 'there is a low volume of reported fraud in the Department.'³²
- 7.42 The Committee notes that Defence assets and operating expenses constitute a substantial part of the Commonwealth's assets and outlays. Ongoing problems with Defence's ability to account for its assets is of concern to the Committee. While **reported fraud** is said to be statistically low, continued poor accounting and controls provides the opportunity for fraud to occur and remain undetected.

The use of the taxation liability method for estimating taxation revenue

- 7.43 The CFS for 2001–02 was prepared, as in past years, using the TLM which recognises taxation revenue when tax payments are due and payable. The method does not conform to AAS 31 *Financial Reporting by Governments* because all taxation revenue, assets and liabilities are not recognised in the period when the underlying transactions occurred.
- 7.44 In contrast, the Australian Taxation Office (ATO) accounted for taxation revenue on an accruals basis using the economic transactions method (ETM). This method recognises taxation revenue when the economic

30 Mr Lloyd Bennett, *Transcript*, 30 April 2003, p. 41.

31 Ms Ann Thorpe, *Transcript*, 30 April 2003, pp. 41–2.

32 Mr Michael Watson, *Transcript*, 30 April 2003, p. 42.

activities raising the tax liability occur and take account of any estimated refunds and/or credit amendments to which taxpayers might be entitled. The ETM meets the requirements of AAS 31.³³

- 7.45 The difference between TLM and ETM is that under ETM, taxation revenue is recognised earlier in the taxation cycle. In a growing economy the consequence is that ETM revenue would generally be higher than TLM revenue.³⁴
- 7.46 The ANAO concluded that for the 2001–02 financial year the operating result was overstated by \$2.8 bn and the net liabilities were overstated by \$7.6 bn. The audit report noted that the use of the TLM was consistent with the treatment adopted for the 2001–02 Budget. As well, while Finance and Treasury did not take the view that ETM provided a reliable measure of taxation revenue, they recognised the comparable reliability of the two methods should be reviewed in future years.
- 7.47 Because the CFS was compiled using the TLM, which did not conform to AAS31, it received a qualification from the ANAO. ATO's financial statements were unqualified on this issue.³⁵
- 7.48 The ATO told the Committee that the ETM required a greater level of estimation than the TLM. However the variance between the two methods was reducing as regards GST revenue because the quarterly activity statements reduced the delay between the point when the liability was accrued and when it was recognised.³⁶ The ANAO added that, in contrast, with company tax and individual tax there could be a significant delay between the end of the financial year and the lodgement of a tax return when the liability was recognised.³⁷
- 7.49 Finance quantified the variance when it advised the Committee that in the 2001–02 consolidated statements the ETM value had to be adjusted by \$653 million. While this only represented 0.4% of total revenue, for consolidated statements the level of materiality set by the ANAO was \$350 million.³⁸
- 7.50 Finance explained that this level of materiality was due to public interest in the consolidated statement's bottom line. Where the result could vary

33 Auditor-General, *Audit Report No. 25, 2002–2003*, pp. 27–8.

34 Auditor-General, *Audit Report No. 25, 2002–2003*, p. 28.

35 Auditor-General, *Audit Report No. 25, 2002–2003*, p. 28.

36 Ms Donna Moody, *Transcript*, 30 April 2003, p. 50.

37 Mr Allan Thompson, *Transcript*, 30 April 2003, p. 50.

38 Mr James Kerwin, *Transcript*, 30 April 2003, pp. 51–2.

from plus to minus \$5 billion, a figure of \$653 million would have a significant effect.³⁹

- 7.51 In contrast, the ATO used the ETM for its own financial statements as there was a higher materiality threshold because the figures were in comparison to total taxation revenue.⁴⁰
- 7.52 A supplementary submission from Finance advised that the TLM method had been introduced for the 1998–99 financial year.⁴¹ Finance told the Committee that the two methods were under ongoing review, but that even though the variances between the two methods had improved there was still too great a swing on a materiality basis to allow the approach to be changed. Finance confirmed that was for the Finance Minister to decide whether to revert back to the ETM.⁴²

The accounting treatment of GST revenue

- 7.53 The 2001–02 CFS as in previous years, was qualified because it had been prepared without recognising the Goods and Services Tax (GST) as Commonwealth revenue. The audit report noted the Government's reason as being that the GST was a State tax collected by the Commonwealth in an agency capacity in accordance with the intent of the *Intergovernmental Agreement on the Reform of Commonwealth-State Financial Arrangements*.
- 7.54 However, the ANAO disagreed, arguing that the GST was part of Commonwealth revenue because:
- The GST was imposed under Commonwealth legislation and therefore the Commonwealth controlled the revenue raised.
 - The relativity factor which adjusted the subsequent payments to the States was determined by the Commonwealth Treasurer. Consequently, the distribution of the GST collected would only coincidentally reflect the amount of tax collected in each jurisdiction.
- 7.55 The audit report noted that the financial statement of the ATO reported the GST as a Commonwealth tax and the Treasury financial statement reported the subsequent payments to the States as grant expenses. As well, the Australian Bureau of Statistics treated the GST as a Commonwealth tax for statistical purposes.⁴³

39 Mr Ian McPhee, *Transcript*, 30 April 2003, pp. 53–4.

40 Ms Donna Moody, *Transcript*, 30 April 2003, p. 53.

41 Finance, *Submission No. 14*, p. 5.

42 Mr Ian McPhee, *Transcript*, 30 April 2003, pp. 55–6.

43 Auditor-General, *Audit Report No. 25, 2002–2003*, pp. 29–30.

7.56 At the hearing, Finance acknowledged the treatments by the ATO and Treasury, and noted that there was agreement on the actual amount of tax collected.⁴⁴ However, Finance stated:

... it is the Finance Minister who prepares the whole-of-government accounts, and I think the Government have made it very clear—from their perspective at least—that the GST is not a Commonwealth tax but a State tax. That reflects the treatment, therefore, that is represented in the Government's accounts.⁴⁵

7.57 The Committee believes that in the face of this impasse there is little to be gained from further debate on the issue.

Australian Taxation Office accounting treatment of information technology outsourcing

7.58 The financial statements of the ATO were qualified because it accounted for the lease of its computer equipment as an operating lease. The ANAO considered the lease should be a finance lease under AAS 17 *Leases*. This was because substantially all the risks and benefits had passed from the lessor to the ATO.⁴⁶

7.59 Many Commonwealth entities, including the ATO, had guaranteed the residual value of the equipment on expiry of the lease or where the equipment had become surplus. As such they bore the risk associated with a decline in residual value below that agreed to. Since residual value risk was the most significant risk associated with asset ownership, the ANAO believed such arrangements should be classified as finance leases.⁴⁷

7.60 The audit report noted that in 2001–02 three Commonwealth entities had changed their accounting treatment for these leasing arrangements from operating leases to finance leases. However, six entities had retained the operating lease treatment. Of these only the ATO's lease had a material effect. Hence only the ATO's financial statements had been qualified.⁴⁸

7.61 The ATO told the Committee that the 2001–02 qualification was the third year of qualification and the contract had two more years to run. The ATO added that it had recently exercised a partial option in the contract for a range of services for another two years.⁴⁹

44 Finance, *Transcript*, 30 April 2003, pp. 46–7.

45 Finance, *Transcript*, 30 April 2003, p. 46.

46 Auditor-General, *Audit Report No. 25, 2002–2003*, p. 36.

47 Auditor-General, *Audit Report No. 25, 2002–2003*, p. 44.

48 Auditor-General, *Audit Report No. 25, 2002–2003*, p. 44.

49 Ms Donna Moody, *Transcript*, 30 April 2003, pp. 42–3.

- 7.62 In determining the accounting treatment, the ATO had received a range of legal advice. The ANAO responded that it had looked at the ATO's legal advice, but it was 'still of the opinion that their IT assets are a finance lease.'⁵⁰
- 7.63 The ATO advised the Committee that its accounting treatment did not materially affect ATO's statement of financial performance. (A supplementary submission from the ATO indicated that the cumulative effect on operating expenses for the three years of the lease was an understatement of \$375 000.⁵¹) However, the ANAO had considered the ATO's assets to be understated by about \$46 million with liabilities similarly understated. These figures were not disclosed in the financial statements.⁵²
- 7.64 In renewing the lease, the ATO told the Committee that it was considering whether any developments warranted a change in the accounting treatment.⁵³ The Committee suggested that the wording of the renewed lease could be clarified to confirm where the risks actually lay. The ATO responded that the issue was:
- ... whether we can do that in a way that does not cost the Commonwealth any more money and does not impact on the services or any of the other things in the contract.⁵⁴
- 7.65 The Committee notes that to date there appear to have been few major problems with the outsourcing arrangements for ATO's IT. However, it is only when such problems arise that the underlying risk of the contract will become apparent. Nevertheless, the Committee believes it would be prudent if the ATO took advantage of the renewal of the lease to resolve the disagreement with the ANAO.

Recommendation 5

- 7.66 **The Australian Taxation Office should review the terms of its information technology outsourcing contract when the contract is renewed so that the nature of the lease is clarified and the subsequent accounting treatment does not attract an audit qualification.**

50 Ms Donna Moody, Mr Allan Thompson, *Transcript*, 30 April 2003, p. 44.

51 ATO, *Submission No. 12*, p. 1.

52 Ms Donna Moody, *Transcript*, 30 April 2003, pp. 42-3.

53 Ms Donna Moody, *Transcript*, 30 April 2003, p. 43.

54 Ms Donna Moody, *Transcript*, 30 April 2003, p. 44.

Audit Report No. 27, 2002–2003

Commonwealth Guarantees, Warranties, Indemnities and Letters of Comfort

Introduction

- 8.1 Guarantees, warranties, indemnities and letters of comfort are types of contingent liabilities which may become actual liabilities if certain events occur, or do not occur. These types of instrument are used in both the public and private sectors to facilitate operations. However, they can carry with them risks and obligations which may be called on in the future, and hence need to be managed throughout the lifetime of the agreement they cover.

Background

- 8.2 Contingent liabilities can be issued in accordance with statutory responsibilities, such as the Treasurer's power to guarantee borrowings. Ministers also have the power under the Constitution to issue such instruments. Nevertheless, Parliament is not bound to provide funds to satisfy such obligations unless there is an existing standing appropriation.

8.3 The framework for issuing and reporting these types of instruments is comprised of two major components, namely:

- an institutional regime which includes:
 - ⇒ relevant Constitutional and legislative provisions;
 - ⇒ Finance Circular No. 1997/06 *Potential Liabilities and Losses*;
 - ⇒ departmental and agency risk management plans; and
 - ⇒ Chief Executive's Instructions; and
- a disclosure regime which includes:
 - ⇒ the *Charter of Budget Honesty Act 1998*;
 - ⇒ the Budget Statement of Financial Risks; and
 - ⇒ annual reporting by departments and agencies.¹

8.4 *Audit Report No. 27, 2002–2003* was a follow-up to two previous audits in 1996 and 1998.² These audits had contained a total of 22 recommendations to which agencies had agreed.³

The audit

8.5 The audit specifically excluded contingent liabilities, which did not explicitly involve the Commonwealth in a legal obligation. This was because they did directly constitute legal contingent liabilities of the Commonwealth. Also excluded were other contingencies, such as uncalled capital subscriptions for multilateral financial institutions and instruments issued by Statutory Marketing Authorities and Government Business Enterprises that did not explicitly involve the Commonwealth in a legal obligation.

8.6 The audit commenced with a questionnaire to 17 departments and 30 agencies to gather information on all explicit Commonwealth contingent liabilities. A sample of departments and agencies were selected for interviews, file review, and further exchange of correspondence.

8.7 The objectives of the audit were to assess, with respect to contingent liabilities:

1 Auditor-General, *Audit Report No. 27, 2002–2003, Management of Commonwealth Guarantee, Warranties, Indemnities and Letters of Comfort*, Canberra, January 2003, p. 12.

2 Auditor-General, *Audit Report No. 6, 1996–97, Commonwealth Guarantees, Indemnities and Letters of Comfort*, Canberra 1996; Auditor-General *Audit Report No. 47, 1997–98, Management of Commonwealth Guarantees, Indemnities and Letters of Comfort*, Canberra, 1998.

3 Auditor-General, *Audit Report No. 27, 2002–2003*, p. 11.

- the action in relation to the recommendations from *Audit Report No. 47, 1997–98, Management of Commonwealth Guarantees, Indemnities and Letters of Comfort*;
- the extent of improvement in agencies' management and monitoring of the Commonwealth's exposure;
- the changes in the size and nature of the Commonwealth's reported exposure since 30 June 1997; and
- the approach of agencies to effective risk management and control of Commonwealth exposures.⁴

Audit findings

- 8.8 The ANAO found that since 30 June 1997 the total quantifiable exposures had almost halved to about \$114.9 billion. Instruments as at 30 June 2002 comprised:
- loan guarantees of \$5.9 billion;
 - non-loan guarantees of \$69.2 billion;
 - indemnities of \$39.7 billion; and
 - letters of comfort of \$110 million.⁵
- 8.9 Over the period the composition of contingent liabilities had changed markedly with non-loan guarantees falling by two-thirds and indemnities rising some thirteen-fold—from \$3.1 billion in 1997 to \$39.7 billion in 2002. The rise in was associated with war risk cover following the terrorist events of 11 September 2001. The audit report noted that indemnities relating to terrorism events was likely to increase further.
- 8.10 The audit revealed that there had been a significant improvement in the number of departments reporting the introduction of structured risk management since the 1998 audit. Over three-quarters of responding departments and agencies reported that they had a corporate risk management plan. However, of those that did, only four entities reported that there was an explicit link between their corporate risk management plan and the management of their contingent liabilities. The ANAO concluded that this should be rectified especially where substantial potential liabilities were involved.

4 Auditor-General, *Audit Report No. 27, 2002–2003*, pp. 12–13.

5 Auditor-General, *Audit Report No. 27, 2002–2003*, p. 13.

- 8.11 The audit found that while there was a high degree of awareness amongst entities to the Finance Circular⁶ concerning contract vetting, authorisation, subrogation, time limits, financial limits and termination clauses, there had not been high levels of compliance with the guidelines it provided. This was especially so in relation to capping liabilities and incorporating termination clauses and time limits. The ANAO considered this potentially exposed the Commonwealth to unnecessary risk, and issuing entities should raise awareness of the importance of sound procedures in the preparation and management of these instruments.⁷
- 8.12 The ANAO made three recommendations to which the audited agencies agreed.⁸

The Committee's review

- 8.13 Four agencies involved with the audit were invited to give evidence to the Committee at a public hearing on Wednesday, 30 April 2003. The agencies were:
- the ANAO;
 - the Finance;
 - the Department of the Treasury (Treasury); and
 - the Department of Transport and Regional Services (DoTARS).
- 8.14 The Committee took evidence on the following issues:
- the accuracy of agency registers of contingent liabilities;
 - the management of risk associated with raising a contingent liability; and
 - accountability to the Parliament.

The accuracy of agency registers of contingent liabilities

- 8.15 During audit fieldwork, the ANAO found that many entities had out of date or inaccurate registers. Inaccuracies ranged from omissions of instruments to inclusions of items which were found not to be contingent liabilities.⁹

6 Finance Circular 1997/06 *Potential Liabilities and Losses*.

7 Auditor-General, *Audit Report No. 27, 2002–2003*, pp. 13–14.

8 Auditor-General, *Audit Report No. 27, 2002–2003*, pp. 19–20.

9 Auditor-General, *Audit Report No. 27, 2002–2003*, p. 43.

- 8.16 The Committee questioned agencies at the public hearing concerning the accuracy of their contingent liability registers.
- 8.17 DoTARS responded that it had a 'central indemnity register which contains copies of all current and past indemnities' which was believed to be complete. In one or two instances of old indemnities the original certified document had not been located, but the department had a copy.¹⁰
- 8.18 Treasury told the Committee that it had a comprehensive electronic records register. While this held copies of all documentation, the originals were located in program areas. However, the current updating of Treasury's chief executive instructions would ensure that all original documents would be consolidated in a central location.¹¹
- 8.19 Finance reported that it kept a register of contingent liabilities which was reviewed on a quarterly basis and presented to the management board for review. It was updated and reviewed annually as part of the preparation of the department's financial statements.¹²
- 8.20 However, after the hearing Finance advised the Committee that several contingent liabilities and their supporting documentation were unaccounted for. They had been lost during the merger of the former Department of Administrative Services and Office of Asset Sales and Commercial Support/Office of Asset Sales and Information Outsourcing into Finance.¹³ Later, a further submission advised that all but one of the 73 contingent liabilities held by Finance had been located. The missing indemnity related to the sale of Australian Airlines in 1991.¹⁴

The management of risk associated with raising a contingent liability

- 8.21 The Committee questioned witnesses as to how their agencies attempted to improve their risk profile before signing the documents which created a contingent liability.
- 8.22 DoTARS outlined its risk management procedures relating to the contingent liabilities arising from the September 11, 2001 terrorist attacks. The indemnities were all risk managed in accordance to the elements outlined in Finance Circular 1997/06 which recommended:
- a financial limit;

10 Mr Jeremy Chandler, *Transcript*, 30 April 2003, p. 66.

11 Mr Bede Fraser, *Transcript*, 30 April 2003, p. 67.

12 Mr Dominic Staun, *Transcript*, 30 April 2003, p. 66.

13 Finance, *Submission No. 8*, p. 1.

14 Finance, *Submission No. 17*, p. 1.

- a time limit;
 - subrogation so that the Commonwealth can pursue recovery against third parties; and
 - termination clauses.¹⁵
- 8.23 DoTARS also told the Committee that the nature of the September 11 event resulted in some of the assessment being conducted in parallel rather than prior to the issuing of indemnities. However, an additional way was used to manage the risk. The major reason for the indemnities was the withdrawal of cover by the insurance market, but as cover returned the department had ‘moved to having a large offsetting insurance policy in front of the Commonwealth’s step-in and payments under the indemnity.’¹⁶
- 8.24 Finance told the Committee that some of its indemnities were not capped. This was because in some cases it had not been possible to establish a financial limit. Finance provided as an example, the costs arising from redressing any environmental pollution when railways and associated land had been sold. However, in this instance the purpose of the indemnity had been confined.¹⁷
- 8.25 A supplementary submission from Finance advised that recently three uncapped indemnities had been issued:
- to the board members of Bankstown Airport Ltd, Camden Airport Ltd and Hoxton Park Airport Ltd against claims and costs arising from the conduct of directors in relation to the sale of those airports;
 - to the board of the Australian Submarine Corporation (ASC) for claims associated with the execution of a services agreement between the ASC, Defence, Electric Boat Corporation and Electric Boat Australia; and
 - to the Chief Executive Officer of Employment National to protect against civil claims relating to employment and conduct as an officer.¹⁸
- 8.26 Treasury drew attention to two of the contingent liabilities of the department which were uncapped:
- in relation to collapse of the HIH Insurance Group, the indemnities covered the subsidiary of the Insurance Council and its employees relating to liabilities arising from their managing the assistance scheme;

15 Mr Simon Clegg, *Transcript*, 30 April 2003, p. 67.

16 Mr Simon Clegg, *Transcript*, 30 April 2003, p. 67.

17 Mr Jeremy Chandler, *Transcript*, 30 April 2003, p. 68.

18 Finance, *Submission No. 14*, p. 7.

- to the Housing Loan Insurance Commission to meet the liabilities arising from the 'old book' policies that the Commonwealth wrote; and
 - to the provisional liquidator of United Medical Protection Ltd and Australasian Medical Insurance Ltd (UMP-AMIL) guaranteeing 'certain aspects of the UMP-AMIL operations.'¹⁹
- 8.27 The Committee has noted in the previous chapter that the uncertainty surrounding two of these indemnities had resulted in the qualification of Treasury's financial statements and the Commonwealth's Consolidated Financial Statements in 2001–02.
- 8.28 The Committee considers that the issuing of uncapped contingent liabilities should be kept to a minimum. Where such liabilities are issued they should be subject to thorough risk management processes which should be well documented for accountability purposes.

Accountability to the Parliament

- 8.29 The audit report drew attention to the parliamentary accountability procedures for the issuing of indemnities adopted by the United Kingdom Parliament.
- 8.30 Where an Act did not outline reporting arrangements and the potential liability could exceed £100 000 (A\$270 000), Treasury approval must be sought before laying a 14 day disallowable minute before the House of Commons. A copy of the minute must also be sent to the Public Accounts Committee and the relevant departmental select committee. If a Member of Parliament objects in writing, Parliamentary Question or Early Day Motion, the guarantee 'is normally not given until the letter or question has been answered.'
- 8.31 In cases of special urgency and a guarantee has to be provided before 14 days, an explanation has to be contained within the minute. As well, if a contingent liability raised commercial confidentiality, national security, or where knowledge of a guarantee could prompt claims from third parties, the matter may be reported in confidence to the Chair of the UK Public Accounts Committee.²⁰
- 8.32 The Committee commented that the UK model provided the opportunity for the UK Parliament to become involved at an early stage in the creation of contingent liabilities. This contrasted with the system in Australia where contingent liabilities were reported after the event.

19 Mrs Bernadette Welch, *Transcript*, 30 April 2003, p. 69.

20 Auditor-General, *Audit Report No. 27, 2002–2003*, pp. 27–8.

8.33 Finance responded:

In the Budget papers and also in the Mid-Year Economic and Fiscal Outlook, the [Australian] Government sets out a statement of all contingent liabilities greater than \$20 million within the year or \$14 million over the forward estimates period. ... and that is consistent with the Charter of Budget Honesty. Then ... departments in their own agency reports disclose all material contingent liabilities and even remote contingencies in their accounts. ... The UK approach is slightly different and it is arguably a more timely approach, but it is not necessarily as comprehensive, on the face of it, as ours.^{21 22}

- 8.34 Finance also highlighted the opportunity in the UK for urgent indemnities to 'bypass' the 14 day disallowance period. It commented that the department fully accepted the view that in Australia 'these instruments need to be controlled' and added that it was up to the Parliament to eventually decide to support any contingent liability by an appropriation.²³

Committee comment

- 8.35 The Committee notes that the audit report identified some 341 contingent liabilities existing in 2002. All but eighteen are greater than the reporting threshold used in the UK and 190 are either unlimited or unspecified.²⁴
- 8.36 In its *Report 350* the then Joint Committee of Public Accounts (JCPA) recommended that:

Full statements of off-balance sheet contingent liabilities associated with guarantees, indemnities and letters of comfort should be a mandatory inclusion in annual financial statements of departments except where disclosure may adversely affect the Commonwealth's interests.²⁵

21 Mr Ian McPhee, *Transcript*, 30 April 2003, p. 70.

22 The requirement for agency annual reports to contain a list of contingent liabilities arose from the Government response to the Committee's recommendation in its

23 Mr Ian McPhee, *Transcript*, 30 April 2003, p. 71.

24 Auditor-General, *Audit Report No. 27, 2002-2003*, pp. 69-84.

25 JCPA, *Report 350, Review of Auditor-General's Reports 1996-97 First Quarter*, Canberra, 1997, Recommendation 2, p. 27.

- 8.37 The Government accepted the JCPA's recommendation and added to the reporting requirement 'any other relevant material contingency that may result in gain or loss to an entity.'²⁶
- 8.38 Notwithstanding the reporting mechanism currently in place in Australia, the Committee considers there is merit in the earlier involvement of Parliament in the issuing of indemnities. The procedure in the UK seems a good model to follow. However, the Committee believes that the threshold adopted in the UK is too low and should instead be that currently in place for the Government's statement of contingent liabilities in the Budget papers and the Mid-Year Economic and Fiscal Outlook.

Recommendation 6

- 8.39 **The Commonwealth should adopt procedures for notifying the Parliament of the issuing of indemnities based on the procedures used by the United Kingdom Parliament.**

26 Department of Finance, *Finance Minute to Report 350*, September 1997, p. 12.

Audit Report No. 20, 2002–2003

Employee Entitlements Support Schemes

Introduction

Background

- 9.1 In January 2000, the Federal Government established the Employee Entitlements Support Scheme (EESS) to provide a safety net for employees who had lost their jobs as a result of their employer's insolvency or bankruptcy. EESS provided government-funded part payment of certain entitlements to affected employees and was administered by the Department for Employment and Workplace Relations (DEWR). The Commonwealth Government funded half the amounts and invited State and Territory Governments to fund the other half. The State Government of South Australia joined the scheme in August 2001.¹

1 Minister for Employment, Workplace Relations and Small Business, Hon Tony Abbott MP, *Media Release, South Australia joins Federal Government scheme to protect worker entitlements*, 6 August 2001.

- 9.2 The collapse of Ansett in September 2001 prompted the Government to announce a special scheme to assist employees whose employment was terminated as a result of the collapse. This scheme was the Special Employee Entitlement Scheme for Ansett group employees (SEESA). At the same time the Government announced a replacement scheme for EESS called the General Employee Entitlements and Redundancy Scheme (GEERS). GEERS was fully Commonwealth funded and provided a higher proportion of the unpaid entitlements than EESS.
- 9.3 EESS was applied to termination resulting from employer redundancies that occurred in the period from 1 January 200 to 11 September 2003. GEERS applied to terminations resulting from employer insolvencies that occurred after 12 September 2001.² SEESA operated under different guidelines to both EESS and GEERS and was the subject of a separate performance audit, due for tabling in 2003.
- 9.4 To 30 June 2002, DEWR had made 8358 EESS and 4582 GEERS payments to employees. At that point the department was receiving approximately 1000 new claims each month in total across both schemes. In 2001-02, total budget expenditure on EESS and GEERS was \$62.36 million. In 2002-03 (which will be the first full year of operation of GEERS), the budget estimate is \$85.183 million, which also includes any residual expenditure on EESS.³
- 9.5 Neither EESS nor GEERS were legislatively based but rather were established by ministerial authority. They were described as 'safety net' schemes only, meaning that although they assist employees who have been affected by employer insolvency, the schemes did not necessarily compensate employees for all their unpaid entitlements.
- 9.6 To gain assistance, potentially eligible individual employees are required to complete a claim form for the schemes. The claims are lodged with DEWR usually through the insolvency practitioner appointed to manage the affairs of the insolvent business. After assessment, DEWR provides an advance to the insolvency practitioner, who after making necessary deductions, such as income tax, distributes the net payments to the former employees.
- 9.7 The operation of both EESS and GEERS were characterised by rapid change and development since the inception of the first scheme. A further administrative challenge has been the inherently unpredictable workload.
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2 Auditor -General, *Audit Report No. 20, 2002-2003, Employee Entitlement Support Schemes*, Canberra, December 2002, p. 11.

3 Auditor-General, *Audit Report No. 20, 2002-2003*, p. 11.

The audit

- 9.8 The objective of the audit was to determine whether DEWR was efficiently and effectively managing the provision of funds to eligible employees under EESS and EERS. This included consideration of whether:
- the eligibility and entitlements of claimants were accurately and cost-effectively assessed;
 - performance information was timely and relevant;
 - there was a strategy to provide clear, correct and timely information to those involved in the scheme; and
 - DEWR had recovered the amounts due from insolvent employers on behalf of the Commonwealth.
- 9.9 The operation of SEESA was not included in the audit.⁴

Audit findings

- 9.10 The ANAO identified a range of opportunities for improvement in the administration of EESS and GEERS. The main area in which DEWR's performance had not been meeting expectation was in the timeliness of making payments under the schemes. Other aspects of the management and operation of the schemes which needed improvement included:
- better management of the administrative framework;
 - enhancement of the range of performance indicators;
 - greater development of the capacity to track and control the processing of cases; and
 - more vigorously pursuing recovery of funds from the assets of insolvent businesses.⁵
- 9.11 The ANAO recognised that in implementing EESS in March 2000, DEWR put in place the first ever publicly funded scheme in Australia as a safety net for employee entitlements upon business insolvency.
- 9.12 The audit report acknowledged that DEWR was responsive to the issues raised by the audit and that it had sought to improve its administration of the schemes as a result. DEWR accepted all nine of the recommendations made by the ANAO.

4 Auditor-General, *Audit Report No. 20, 2002–2003*, p. 12.

5 Auditor-General, *Audit Report No. 20, 2002–2003*, p. 13.

The Committee's review

- 9.13 On 21 May 2003, the Committee held a public hearing to review DEWR's progress in implementing the ANAO's recommendations.
- 9.14 The Committee took evidence on the following issues:
- the administrative framework of the schemes;
 - the timeliness and management of processing;
 - relationship management ;
 - funding arrangements; and
 - recovery from assets.

Administrative framework

- 9.15 The audit report highlighted concerns with the administrative framework in which the schemes were operating. The ANAO described the problems generally:
- ... it was not a well-managed program. A number of administrative weaknesses were identified and, to DEWR's credit, it had taken action to address them. But it was not a well-managed program.⁶
- 9.16 One of the main ANAO criticisms was that DEWR lacked the processes necessary for maintaining consistency in key decision-making. The report stated:
- The ANAO found no evidence that key decisions were being systematically documented or made known to the whole branch. ... this meant that there was no reliable mechanism for ensuring that each of the people occupying delegate positions over time was aware of a potentially important and precedent setting decision made by another. There is a risk ... that different delegates could take different positions and that consistency in decision-making and equitable treatment of claimants might not be maintained.⁷
- 9.17 DEWR responded that it had set up the Case Manager intranet portal that provided relevant information and advice for all staff. To ensure staff were alerted to new decisions or changes in procedure, 'process alerts' were emailed to all staff as well as being posted on the intranet. In addition,

6 Mr John Meert, *Transcript*, 21 May 2003, p. 77.

7 Auditor-General, *Audit Report No. 20, 2002-2003*, p. 44.

DEWR noted that its procedural guidelines were updated whenever such a process alert was issued.

9.18 DEWR maintained that this improvement had been undertaken during the audit and asked the Committee to note that the ANAO had witnessed a number of process alerts during their field work.

9.19 DEWR indicated that, in response to the audit report, it had hired a consultant to review the business model and generally address problems associated with the administrative framework.⁸

9.20 The Committee expressed interest in the findings of the consultant and DEWR provided details of the findings in a supplementary submission. The consultant suggested the following actions:

- the design of a preferred service delivery model and the associated re-engineering strategy;
- the development of an implementation strategy, including the creation of a separate Employee Entitlements Projects Branch;
- the establishment of a separate departmental output for the administration of GEERS, including third party outputs;
- the continuation of liaison with Finance in relation to the use of the special account for GEERS; and
- the development of a proposed approach to preparing the budget estimates for 2003–04.⁹

9.21 DEWR informed the Committee that all the consultant's recommendations had been accepted and were being implemented.¹⁰

Cost of administering the schemes

9.22 The Committee expressed concern at the cost of administering the schemes. In particular, the Committee noted that there were conflicting understandings between DEWR and the ANAO over the nature of a cap that was to be applied to the administrative costs of the schemes.

9.23 The Committee, in examining the budget references to the schemes, noted that a departmental appropriation of \$9.469 million was expected for the year 2003–04. However, this figure was not in keeping with the \$5 million

8 Mr Michael Maynard, *Transcript*, 21 May 2003, p. 90.

9 DEWR, *Submission No. 18*, p 4.

10 DEWR, *Submission No. 18*, p 4.

per year cap on administrative costs negotiated between DEWR and Finance.

9.24 DEWR explained its understanding of the position:

The \$5 million negotiated with Finance was for a particular year – not last year, the year before. It was only a notional indicative amount. It has never been a budget item to which we are limited.¹¹

9.25 ANAO disagreed with this position, stating that it was their understanding that the \$5 million per year cap was to be an ‘ongoing rate’.¹²

9.26 The Committee was concerned with ascertaining an accurate figure for expenditure on administration and some explanation as to why this figure had increased significantly.

9.27 DEWR’s response included reference to a new information technology support system, costed at approximately \$1 million as well as costs associated with the implementation of a new business model.¹³ The department subsequently provided information that \$12.9 million had been expended on administration costs since the commencement of the schemes in 2000 up to 30 May 2003.¹⁴

Committee comment

9.28 The Committee notes that the administration of both EESS and GEERS has been a major challenge for DEWR as these schemes are the first of their kind in Australia. The Committee also notes that the nature of the schemes’ application meant that they involved a further administrative challenge of a highly unpredictable workload.

9.29 The Committee commends the department on its positive response to suggestions for improvement from both the ANAO and DEWR’s consultant and notes that many of the ANAO’s suggestions and recommendations have already been partially or fully implemented.

9.30 However, the Committee is concerned at the increasing costs associated with the administration of the schemes and expects improvement in this area. Full implementation of the ANAO recommendations will contribute to DEWR’s ability to effectively administer both of the schemes.

11 Ms Malisa Golightly, *Transcript*, 21 May 2003, p. 95.

12 Mr David Rowlands, *Transcript*, 21 May 2003, p. 95.

13 Mr Michael Maynard, *Transcript*, 21 May 2003, p. 83.

14 DEWR, *Submission No. 18*, p. 9.

- 9.31 The Committee notes the audit report's suggestion that DEWR measure and report on the trend in the mean administration cost of making each payment and is pleased to learn that this data should be available by the end of the 2002–2003 financial year.

Timeliness and management of processing

- 9.32 The timeliness of delivering employee benefits was always a key consideration in the design and operation of both EESS and GEERS. The audit report quoted the ministerial statement of January 2001, Protection of Employee Entitlements on Employer Insolvency:

In the past, workers who have not received their full entitlements on their employers' insolvency have been left in the queue of creditors under the Corporations Law. This has meant many employees were not paid monies owed, with no safety net *that would have enabled the quick payment of at least some of these entitlements* [ANAO's emphasis].¹⁵

- 9.33 The ANAO identified that the Commonwealth in this instance was assuming two risks. The most obvious risk assumed is that of the employee not being paid at all. The second risk was that in endeavouring to pay employees 'up front', clearly the Commonwealth had the intention to pay the employees promptly and then assume the risk of collecting monies owed at a later date.
- 9.34 For these reasons, the ANAO gave particular attention to the performance criterion of timeliness of processing and found that DEWR faced 'substantial challenges in making prompt payments under the EESS and GEERS schemes'.¹⁶
- 9.35 The audit report noted that DEWR had originally set targets of 12 weeks for completion of claims processing.¹⁷ However an internal evaluation report had concluded that the 12 week target was not realistic and this had been modified to 16 weeks.¹⁸
- 9.36 The Committee questioned DEWR about progress in relation to these targets, noting that the audit report stated that, overall, DEWR had taken 26 weeks to clear 80 per cent of the claims, well short of the original

15 Auditor-General, *Audit Report No. 20, 2002–2003*, p. 74.

16 Auditor-General, *Audit Report No. 20, 2002–2003*, p. 86.

17 Auditor-General, *Audit Report No. 20, 2002–2003*, p. 75.

18 Auditor-General, *Audit Report No. 20, 2002–2003*, p. 75.

published standard of 80 per cent in 12 weeks and still well short of the revised target of 80 per cent in 16 weeks.¹⁹

9.37 At the hearing DEWR reported that its average response time in 2002–03 was 65 per cent in 16 weeks and the latest monthly performance had been 74 per cent in 16 weeks. On average, it reported achieving 80 per cent clearance in 22 weeks

9.38 DEWR explained the delay in payments:

The time frames within which a payment can be made are affected not only by the department's efficiency but also by the capacity for insolvency practitioners to provide us with verified employee entitlements data. ... In some cases it takes months for insolvency practitioners to determine [employee entitlements]. That time is counted as part of the time frames that a claim sits on our books and consequently, is recorded in our statistics.²⁰

9.39 When asked to explain what the department was doing to improve the timeliness of claims processing, DEWR listed the following improvement strategies:

The number of persons available to work on this has been increased. The number of accountants has been increased. Our processes are constantly under review to ensure we are having the most efficient means possible. We seek to inform insolvency practitioners about the scheme and the requirements of the scheme so they can provide us with the information quickly. Most significantly, there is the current business re-engineering process that we are going through, including the market testing of some elements of the administration of the scheme.²¹

Timeliness of appeals

9.40 The audit report noted that the number of appeals against EESS and GEERS decisions rose during the first six months of 2002. It also reported that DEWR was taking longer than its target time to resolve most appeal cases.²²

9.41 DEWR reported that it had taken steps to improve the appeals process. This included the establishment of a quality assurance team to deal with

19 *Transcript*, 21 May 2003, p. 78.

20 Mr Michael Maynard, *Transcript*, 21 May 2003, pp. 77–8.

21 Mr Michael Maynard, *Transcript*, 21 May 2003, pp. 98–9.

22 Auditor-General, *Audit Report No. 20, 2002–2003*, p. 15.

appeals and inquiries from the ombudsman as well as general quality assurance processes and improvements.²³

9.42 The Committee expressed concern about the independence of such a team if working within the branch dealing with case management.

9.43 DEWR stated that the independence of this team was assured by its 'completely separate management structures' and the clearly separate functions between the quality assurance team and the case management team.²⁴

9.44 On being questioned about time taken to resolve appeals, DEWR reported a median duration for appeal resolution of 45 days, with the shortest time being 1 day and the longest delay being 12 months.²⁵

9.45 DEWR also reported that they were well within targets of greater than 97 per cent of claims not being varied after appeal. Their actual figures were disclosed:

We have had 853 appeals over the life of the program, of which 160 have resulted in the original decision being overturned. That represents 0.6 of one per cent of all the decisions taken by the department in relation to this program.²⁶

Committee comment

9.46 The Committee acknowledges the unique demands upon the department in managing an unpredictable workload in a sensitive environment. However, the Committee is keen to see DEWR implement fully recommendations made by the ANAO to improve the management of the schemes.

9.47 The Committee is pleased to note that DEWR has taken steps to implement the recommendation of the establishment of a quality assurance team. The Committee looks forward to better processes for management arising from the work of this team.

9.48 From the figures provided by DEWR concerning the number of successful appeals, the Committee calculates that 3.2 per cent of the department's decisions are appealed. In such a challenging environment where tough decisions have to be made, there will always be some decisions which will

23 Mr Michael Maynard, *Transcript*, 21 May 2003, p. 79.

24 Mr Michael Maynard, *Transcript*, 21 May 2003, p. 80.

25 DEWR, *Submission No. 18*, p. 3.

26 Mr Michael Maynard, *Transcript*, 21 May 2003, p. 81.

be appealed. The Committee expects DEWR to use its quality assurance mechanism to ensure that the vast majority of its decisions can withstand any appeals process.

- 9.49 The Committee considers that timeliness of payment for both schemes must be a paramount consideration for the department. As both the EESS and the GEERS are designed to act as 'safety net' schemes, it is incumbent upon DEWR to ensure that employees affected by company insolvency have access to funds as quickly as possible. The Committee looks forward to DEWR meeting its targeted timeframes for claims processing time.

Relationship management

- 9.50 The audit report examined the relationships between DEWR and both EESS and GEERS claimants and between DEWR and insolvency practitioners as both these relationships are central to the efficient and effective management of the schemes.

- 9.51 The audit report noted that:

For the scheme to be working effectively and providing good service, claimants need to be ... aware of the assistance available and how to seek it [and] generally aware of what happens once they have lodged a claim, especially where there are often claimant expectations of immediate outcomes that are not likely to be realised.²⁷

- 9.52 The Committee questioned DEWR about how it managed awareness of the scheme and subsequently monitored claimants' understanding of the process. The Committee expressed concern that, on occasion, information about the scheme did not 'filter down' to potential claimants and that this potentially disadvantaged people in an already difficult situation.²⁸

- 9.53 DEWR explained that it targeted its information material very specifically:

We have found ... that the best method is to target those people who are directly involved in the process—direct correspondence with insolvency practitioners and accountants; availability of the information through Centrelink for persons who unfortunately find themselves made redundant; through the department's wage line and our hotline; and ensuring that all of the peak industry bodies and unions are made aware of the existence of the scheme.²⁹

27 Auditor-General, *Audit Report No. 20, 2002–2003*, p. 87.

28 *Transcript*, 21 May 2003, p. 97.

29 Mr Michael Maynard, *Transcript*, 21 May 2003, p. 97.

- 9.54 DEWR did concede that much information distribution relied upon insolvency practitioners and that in spite of this heavy reliance it did little in the way of monitoring interactions between insolvency practitioners and claimants.
- 9.55 In a submission to the Committee subsequent to the public hearing, DEWR explained its plans for improving claimants' understanding of the scheme, particularly relating to the eligibility criteria:
- The department is currently finalising arrangements to focus test GEERS information material, including a revised claim form, in order to ensure that the material is as simple and informative as possible for potential claimants.³⁰
- 9.56 The audit report had identified the heavy reliance upon insolvency practitioners by the department. In light of this reliance, the ANAO suggested that DEWR establish a 'regular consultative arrangement in order to improve communication between the department and insolvency practitioners.'³¹
- 9.57 The Committee enquired about progress of this suggestion.
- 9.58 DEWR reported that it held regular meetings with the Insolvency Practitioners Association of Australia and that it was pursuing the involvement of the state insolvency boards in order to broaden the consultative process.

Committee comment

- 9.59 The Committee recognises that insolvency practitioners have a substantial and essential role in the successful operation of EESS and GEERS. Consequently, DEWR's management of its relationship with insolvency practitioners will have a significant impact on DEWR's management of both EESS and GEERS. The Committee endorses the ANAO's view that it is in the interests of all parties if DEWR strengthens its relationship with insolvency practitioners by formalising contact, possibly through a regular consultative mechanism.
- 9.60 The Committee notes that DEWR works closely with and relies heavily upon the advice of insolvency practitioners, as do employees affected by company insolvency. Claimants may be at a disadvantage without some form of departmental monitoring of the interactions between insolvency practitioners and individual claimants.

30 DEWR, *Submission No. 18*, p. 11.

31 *Transcript*, 21 May 2003, p. 100.

- 9.61 Alternatively, the Committee believes DEWR could take a more active role in promoting awareness of the schemes, the eligibility criteria that apply, and changes in the interpretation of the operational arrangements so that individuals affected by company insolvency can actively pursue options for assistance.

Recommendation 7

- 9.62 **The Department of Employment and Workplace Relations examine ways in which it can:**
- **improve claimants' awareness of the scheme, their eligibility for benefits under the scheme, and changes in the interpretation of the operational arrangements; and**
 - **monitor interactions between insolvency practitioners and individual claimants for the quality and accuracy of information provided to claimants.**

Funding arrangements

- 9.63 The audit report noted that:

... the funding arrangements for EESS and GEERS are unusual in that all funds for the scheme are provided through a special account. This arrangement derives from the original conception of how EESS would operate, with contributions from States and Territories ... However, given that States and Territories are not expected to contribute to GEERS funding it is not clear that a special account remains the most appropriate mechanism for funding arrangements.³²

- 9.64 The Committee expressed concern about the use of the special account to fund GEERS as the replacement of EESS, especially in light of initial legal advice from the Australian Government Solicitor (AGS) that 'the special account established for EESS could not be used for GEERS.'³³
- 9.65 DEWR disputed the interpretation of this advice and explained that it had sought further advice from the AGS in light of the provision of further information. When asked directly why it continued to administer GEERS

32 Auditor-General, *Audit Report No. 20, 2002-2003*, p. 111.

33 Auditor-General, *Audit Report No. 20, 2002-2003*, p. 109.

though the special account after having received legal advice that it should not, DEWR stated:

That advice was subsequently rescinded by the same officer in the AGS who provided it to us on provision of a fuller level of detail as to the context. The initial question did not have all the context of the administration of the schemes within it and, consequently, the advice was then clarified with the AGS who provided subsequent legal advice that it was appropriate to continue to do so.³⁴

9.66 However, the Committee also noted that the legal advice had been accompanied by a suggestion that the determination relating to the EESS special account be amended to clarify the position in relation to GEERS.

9.67 The audit report also noted this as an issue of concern. It quoted from the advice given by the AGS that:

... if GEERS is to be operated from a Special Account in the future I think it would be clearly desirable for the determination relating to the EESS Special Account to be amended to make it clear that the Account can be used for GEERS. Alternatively, a new Special Account could be established for GEERS.³⁵

9.68 The audit report added that were doubts about the appropriateness of the funding mechanism, given that the newer scheme of GEERS was wholly Commonwealth funded (where EESS had had a portion of State/Territory funding). The report stated that, in light of material changes in the operation of GEERS as compared to EESS, the ANAO suggested 'that DEWR ensure the most appropriate funding mechanism is adopted for funding the scheme going forward.'³⁶

9.69 Under close questioning from the Committee, DEWR indicated that it was in discussions with Finance about the best way to proceed.

Committee comment

9.70 The Committee acknowledges that administrative and funding arrangements for the employee entitlements schemes is a largely uncharted area both for DEWR and other relevant agencies.

9.71 However, ensuring absolute clarity of funding arrangements and mechanisms is essential in the interests of clear and transparent accountability for the expenditure of public money.

34 Mr Michael Maynard, *Transcript*, 21 May 2003, p. 84.

35 Auditor-General, *Audit Report No. 20, 2002-2003*, p. 110.

36 Auditor-General, *Audit Report No. 20, 2002-2003*, p. 110.

- 9.72 The Committee urges DEWR to clarify and finalise its position on the funding arrangements for GEERS so as to prevent continuing confusion over the funding mechanisms being utilised.

Recovery from assets

- 9.73 The audit report noted that the recovery of funds by the Commonwealth from the sale of the assets of an insolvent business was an important aspect of the EESS and GEERS schemes. DEWR's role was to pay outstanding entitlements as an advance, with some expectation of recovery. The department only advanced funds in cases where the insolvency practitioner involved formally recognised the Commonwealth as a creditor to the insolvent business. The report noted DEWR's recovery policy with the following statement:

Where taxpayer funds have been distributed under the scheme for the benefit of employees, these should be recovered from insolvent business or bankruptcies wherever possible.³⁷

- 9.74 However, the audit report considered that DEWR's approach to the recovery was unlikely to yield the optimum outcome for the Commonwealth and that there was an untapped potential for the Commonwealth to be 'more attentive to recovery of its debts'.³⁸ It noted that the current practice left the insolvency framework to run its course and it was assumed that the process would provide appropriate amounts to the Commonwealth in due course should there be any realisation of assets.
- 9.75 The Committee sought DEWR's response to the suggestion that it had the capacity to become a more active creditor.
- 9.76 DEWR noted that changes had been made to the department's recovery strategy as a result of the audit report. DEWR explained these changes:

The creation of a separate recoveries unit to manage the recoveries process is a significant improvement that has been put in place. The use of the department's position as a creditor is actively being followed up. We now sit as a member of the committees of inspection on a number of entities where there is the expectation that dividends will be paid and we seek to get further information

37 Auditor-General, *Audit Report No. 20, 2002-2003*, p. 100.

38 Auditor-General, *Audit Report No. 20, 2002-2003*, p. 104.

from insolvency practitioners on a regular basis on the likelihood of repayments.³⁹

- 9.77 The Committee questioned who assumed the role of delegate to the committees of creditors meetings. DEWR indicated that the delegate was usually a department senior executive. However, who attended was influenced by several factors such as:
- the likelihood of a distribution from the entity;
 - the amount of distribution from the entity—where more than \$200 000 was owed to employees, a DEWR senior executive attended creditors meetings; and
 - the status of the entity—whether it was under deed of company; in administration; in liquidation; or in receivership.⁴⁰
- 9.78 The Committee notes that there were a small number of cases referred to in the audit report where insolvency practitioners had refused to recognise a debt to the Commonwealth. This usually occurred in the event of some impropriety on the part of the insolvent business, such as trading while insolvent.⁴¹
- 9.79 The Committee asked for details of the number of such cases and their financial value. DEWR reported that as at 30 May 2003, the department's records showed a total of 47 cases where the Commonwealth had not been recognised as a creditor. \$3.3 million dollars in EESS or GEERS assistance had been advanced to these cases.⁴²
- 9.80 The Committee questioned DEWR on the likely impact on debt recovery from the proposal to make employee entitlements a 'maximum priority' for insolvent companies. DEWR pointed out that the proposal had the potential to decrease the reliance on GEERS as available assets would go directly to employees, who would therefore not need access to a safety net scheme.

Committee comment

- 9.81 The Committee acknowledges that recovery from assets of insolvent companies takes time to achieve. However, evidence presented in the audit report indicates that a more consistent and persistent approach to

39 Mr Michael Maynard, *Transcript*, 21 May 2003, p. 91.

40 Mr Michael Maynard, *Transcript*, 21 May 2003, p. 92.

41 Auditor-General, *Audit Report No. 20, 2002-2003*, p. 103.

42 DEWR, *Submission No. 18*, p. 8.

recovery action would signal to insolvency practitioners the importance of debt recovery to the Commonwealth. It may also increase the amount recovered.

- 9.82 The Committee endorses the ANAO recommendation that DEWR more actively manage the Commonwealth's interests as a creditor in EESS and GEERS cases and is pleased with the actions undertaken to date to improve the rate of recovery from assets. As noted in DEWR's own recovery policy, these schemes are funded with taxpayer's funds and therefore DEWR is under obligation to seek every possible means of recovering funds owed to the Commonwealth. The Committee looks forward to hearing of further progress in this matter.

Audit Report No. 23, 2002–2003

Physical Security Arrangements in Commonwealth Agencies

Introduction

Background

- 10.1 Protective security encompasses information, personnel, physical, information technology and telecommunications security. The Commonwealth's Protective Security Policy is outlined in the Protective Security Manual (PSM) which provides specific guidance to agencies on the protection of the Commonwealth from potential security threats.¹
- 10.2 Part E of the PSM outlines the Commonwealth's physical security policy, including the recommended physical security framework, procedures and minimum standards.

¹ Auditor-General, *Audit Report No. 23, 2002–2003, Physical Security Arrangements in Commonwealth Agencies*, Canberra, December 2002, p. 13.

- 10.3 In recent years, changed work practices such as an increasing reliance on information technology, contracting and home-based work practices have exposed the Commonwealth to new vulnerabilities and risks. In addition the international and domestic security environment has been changed by the impact of events such as the terrorist attacks in September 2001 and the Bali bombings in October 2002. These events have created a heightened awareness of the range of risks to be managed by Commonwealth agencies.
- 10.4 To maintain a secure environment, such risks and vulnerabilities need to be understood, prioritised and managed to prevent the occurrence of harm (defined in the PSM as any negative consequence), such as compromise of or damage to or loss incurred by the Commonwealth.

The audit

- 10.5 The audit evaluated the security policies and practices of seven Commonwealth agencies to determine whether they had established an appropriate physical security control framework based on the principles outlined in the PSM.
- 10.6 Specifically the audit examined whether the agencies had:
- assigned roles and responsibilities for security;
 - undertaken an appropriate Security Risk Assessment process prior to developing the Agency Security Plan;
 - documented and implemented an effective set of controls and procedures to limit the impact and/or consequence of their identified security risks to an acceptable level;
 - educated staff in their responsibilities and duties within the security environment; and
 - considered the risk, and developed an appropriate policy statement on the physical security arrangements for employees who work from home.²

Audit findings

- 10.7 The audit report concluded that all the audited agencies had made reasonable progress towards meeting their physical security responsibilities as outlined by the PSM. In general this resulted in the
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2 Auditor-General, *Audit Report No. 23, 2002–2003*, p. 14.

establishment of a protective security control framework capable of limiting their exposure to physical security risks.

10.8 However, a number of deficiencies were identified which could have had a negative impact upon the integrity of the protective security environment. The report found that agencies were not:

- undertaking regular comprehensive protective security risk assessments;
- formally considering the physical safety of staff as part of the risk assessment process;
- establishing a clear link between the risk assessment process and procedure development;
- maintaining adequate and current documentation to support the security risk, cost benefit analysis and decision-making processes;
- consistently applying internal controls and procedures, thereby undermining their effectiveness;
- educating their staff, contractors and clients of agency security standards; and
- monitoring the effectiveness and cost-efficiency of the security environment and acting on identified deficiencies in a timely manner.³

10.9 The audit report noted that deficiencies in the physical security segment of a protective security framework needed to be considered in conjunction with other aspects of the protective security. This was because an exposure in one part of the framework could result in increased exposure on an agency-wide level.

10.10 The report also noted that the audit was undertaken at a time when Commonwealth agencies were operating in a heightened international threat environment, following terrorist attacks in New York and in Bali. These events added weight to the report's conclusion that agencies needed to move to a proactive protective security approach.

10.11 The report emphasised that Commonwealth agencies now operated in an environment where they were required to acknowledge that threats and risks once thought unlikely must now be considered as possibilities.

10.12 The report's findings were supported the Attorney-General's Department following work undertaken by the Protective Security Coordination

3 Auditor-General, *Audit Report No. 23, 2002–2003*, p. 15.

Centre. The Centre had found that agencies had a weak and reactive approach to maintaining their protective security responsibilities.⁴

The Committee's review

- 10.13 On 21 May 2003, the Committee held a public hearing to review the progress made by the relevant agencies in relation to the implementation of the ANAO's recommendations.
- 10.14 The Committee took evidence from the following agencies:
- Department of Prime Minister and Cabinet (PM&C);
 - AirServices Australia;
 - Australian Nuclear Science and Technology Organisation (ANSTO); and
 - Parliament House Security Board.
- 10.15 The Committee took evidence on the following issues:
- security education and awareness;
 - security risk assessment; and
 - incident management and reporting.

Security education and awareness

10.16 The audit report emphasised that security regimes were only effective if everyone involved in adhering to the requirements was aware of their responsibilities and consistently applied the identified controls. It also noted that agencies were required by the Commonwealth, as documented in the PSM, to ensure that the staff, contractors and clients were made aware of and were regularly briefed on the security requirements of the agency.⁵

10.17 The report stated that:

Agencies should develop education and awareness programs based on the security standards and documented procedures of the agency. These should be communicated to staff when they commence with the agency, and then on a periodic (at least annual) basis thereafter as part of a security refresher awareness

4 Auditor-General, *Audit Report No. 23, 2002–2003*, p. 17.

5 Auditor-General, *Audit Report No. 23, 2002–2003*, p. 48.

program ... Agencies can also make use of information circulars to advise staff, in a timely manner, of new or revised standards.⁶

10.18 The audit found that not all of the agencies provided this level of staff training. Four of the agencies did not provide new starters with training and in five of the agencies involved in the audit, the on going training was found to be 'insufficient, of low quality and not provided to all staff'.⁷

10.19 The Committee questioned the agencies attending the hearing about provision of security training within their organisations.

10.20 All agencies present described processes involving security training in the induction packages of new starters and several indicated that, since the audit, they had begun the practice of refresher security training for all staff. PM&C stated:

Last year we conducted a security awareness refresher course for all staff; that was conducted by the training officers from the Protective Security Coordination Centre. We are proposing that that will be an annual event.⁸

10.21 ANSTO noted that:

We have also had recently ... security awareness seminars for everybody on the site, which involved getting in some expert lecturers from outside the organisation to discuss the various aspects of security.⁹

10.22 AirServices Australia explained the devolution of security responsibility to business centres but outlined procedures that ensured security training was ongoing, even for employees of long standing:

[Business centres] report to us. They provide routine reports ... about the scope and the nature of the training that is conducted and the numbers of people attending. [If they were not including security training] we would remind them of what their obligations are for particular training.¹⁰

10.23 On behalf of the Parliament House Security Board, both the Department House of Representatives and Department of the Senate indicated that they were trialling online security training as an ongoing refresher training option.

6 Auditor-General, *Audit Report No. 23, 2002-2003*, p. 48.

7 Auditor-General, *Audit Report No. 23, 2002-2003*, p. 48.

8 Mr Terry Crane, *Transcript*, 21 May 2003, p. 112.

9 Mr Steven McIntosh, *Transcript*, 21 May 2003, p. 111.

10 Mr Michael Howard, *Transcript*, 21 May 2003, p. 112.

- 10.24 However, Parliament House Security Board also indicated a number of challenges to providing staff with initial and refresher training in security awareness. While departmental staff were catered for by the separate parliamentary departments, Members of Parliament and their staff were not. A representative of the Board explained:

We have quite an issue in communicating with the occupants of [Parliament House] because of their itinerant nature and that is something that we should be taking on board.¹¹

- 10.25 PM&C also highlighted the difficulty in providing time for additional training, and the importance of creating a culture of responsibility among all staff, noting that:

The level of training that we provide to our staff is probably the maximum we could provide under the circumstances. If I were looking to mandate two or three days of training for each member of staff, I would have great difficulty ... Having said that I think we do provide a good balance. People in Prime Minister and Cabinet are well aware of their responsibilities and we do stress to them that I am not the person responsible for security in Prime Minister and Cabinet, each and every person that works in that department is responsible for the security.¹²

Incident reporting and management

- 10.26 The audit report noted that the integrity of the security environment was strengthened where agencies took a proactive approach to the monitoring, response and reporting of incidents that have resulted in a security breach.
- 10.27 The report emphasised that it was crucial for agencies to respond to incidents in a structured, thorough and timely manner. This included the timely recording and investigation of security incidents, analysis of the information gathered for the investigation and incorporation of the information into the agency security plan.
- 10.28 The audit report also noted that only two agencies were able to demonstrate that they enacted any form of discipline for security breaches committed by staff.¹³
- 10.29 At the public hearing the Committee sought clarification from agencies on how they responded to security breaches by staff.
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11 Mr David Elder, *Transcript*, 21 May 2003, p. 114.

12 Mr Terry Crane, *Transcript*, 21 May 2003, p. 116.

13 Auditor-General, *Audit Report No. 23, 2002–2003*, p. 84.

10.30 Agencies explained that they responded to staff security breaches with a range of options, depending upon criteria such as whether the incident was a 'one off' or a repeat offence and the severity of the breach. Agency disciplinary responses included the following:

- placement of letter on personnel file;¹⁴
- request for written explanation of breach;¹⁵
- reference to breaches during performance appraisal;¹⁶
- withdrawal of access;¹⁷ and
- possible dismissal.¹⁸

10.31 The Committee raised the breach of ANSTO's perimeter by Greenpeace protesters on 17 December 2001. The Committee questioned ANSTO on how it had responded to the incident.

10.32 ANSTO pointed out that although the security guards attempted to prevent the breach, they were limited in their powers:

The APS Act limits [guards] from using force unless lives are in peril, basically. They made a judgement on the day that this was a political protest, lives were not in peril and, therefore they were not entitled under their act to use force. We have taken a number of physical security steps since, but we did not see that there was scope for disciplining anybody for that action, because they were prohibited by their Act from doing anymore than they did.¹⁹

10.33 The Committee noted reference in the audit report to the limitations of over-reliance on security guards and that during its fieldwork the ANAO had observed a number of breakdowns in the application of controls by security guards.²⁰The Committee cited incidents of personal experiences where this had also happened.²¹

14 Mr Michael Howard, *Transcript*, 21 May 2003, p. 108.

15 Mr Terry Crane, *Transcript*, 21 May 2003, p. 109.

16 Mr Terry Crane, *Transcript*, 21 May 2003, p. 109

17 Mr Steven McIntosh, *Transcript*, 21 May 2003, p. 109.

18 Mr Michael Howard, *Transcript*, 21 May 2003, p. 108

19 Mr Steven McIntosh, *Transcript*, 21 May 2003, p. 109.

20 *Transcript*, 21 May 2003, p. 107.

21 *Transcript*, 21 May 2003, p. 109.

- 10.34 The audit report also noted that guards may be less effective if, as was observed, they were overloaded with operational and management duties as well as being expected to respond to security breaches.²²
- 10.35 Agencies were asked to comment on these criticisms and responded by explaining the range of controls used to ensure the physical security environment. This included:
- guards placed at high risk points, particularly entry/exit points;
 - surveillance systems, including recording systems and CCTV;
 - electronic alert mechanisms;
 - physical barriers; and
 - reliance on intelligence from Australian Security Intelligence Organisation (ASIO), the Protective Security Coordination centre (PSCC) and the Australian Federal Police (AFP).²³

Security risk assessment

- 10.36 The audit report recommended that all Commonwealth agencies be required to undertake an appropriate and thorough protective security risk assessment process at least every three years.²⁴
- 10.37 However, the PSCC stated that agencies should review and update their security plans and risk assessments on an annual basis, particularly taking account of ad hoc security reviews that may have arisen from security breaches.²⁵
- 10.38 The Committee noted that the audit report criticised agencies for not integrating their learning from ad hoc security assessments into their existing control frameworks.
- 10.39 At the hearing the agencies responded with explanations of risk assessment processes that generally contained similar actions and procedures. For example, PM & C stated:

...we undertake regular internal reviews and also risk assessments, and we have certainly done so since the issuing of the general security alert by PSCC in November 2002. The recommendations of those reviews have been acted upon and we

22 Auditor-General, *Audit Report No. 23, 2002–2003*, p. .

23 *Transcript*, 21 May 2003, pp.107–108.

24 Auditor-General, *Audit Report No. 23, 2002–2003*, p. 44.

25 Auditor-General, *Audit Report No. 23, 2002–2003*, p. 42.

have incorporated much of that into our security plan which was issued in September last year. Since then we have reviewed our internal arrangements on a number of occasions.²⁶

- 10.40 Two of the agencies present indicated that they utilised the PSCC risk management training courses and materials for relevant staff. All indicated that they had formal risk assessment processes that took account of security risk assessment as part of the overall risk asses The Committee is pleased to note that the agencies have responded in a timely and appropriate manner to the recommendation that agencies develop and schedule periodic formal education and awareness programs for all personnel.²⁷

Committee comment

- 10.41 The Committee acknowledges that all agencies have constraints that affect the manner in which they provide security training. Clearly, each agency must look for ways to address the security framework in the most effective and efficient way for the organisation involved. However, it is incumbent upon agencies to ensure that training is relevant, accessible to all staff and maintains staff knowledge to current security standards.
- 10.42 The Committee is pleased to note that agencies are aware of the importance of a thorough and timely response to security breaches and the importance of incorporating learnings gained from breaches into current security controls.
- 10.43 The Committee notes that the ANAO report contains suggestions and examples of better practice which may be of use to Commonwealth agencies in providing a secure physical environment. The Committee encourages agencies to examine the potential lessons in the report.

26 Mr Terry Crane, *Transcript*, 21 May 2003, p. 111.

27 *Transcript*, 21 May 2003, pp. 110–11.

Audit Report No. 28, 2002–2003

Northern Territory Land Councils and the Aboriginal Benefit Account

Introduction

Background

- 11.1 In February 1973, the Commonwealth Government set up a Royal Commission, led by Mr Justice Woodward, to investigate how land rights for Aboriginal people might be achieved in the Northern Territory (NT). Justice Woodward's first report recommended the establishment of two land councils to represent the views of Aboriginal people in the NT. These land councils were the Northern Land Council (NLC) and the Central Land Council (CLC).
- 11.2 Following recommendation in Justice Woodward's second report, the *Aboriginal Land Rights (Northern Territory) Act 1976* (ALRA) was passed in 1976. The ALRA combined concepts of traditional Aboriginal law and property rights associated with land ownership. Under the ALRA, traditional owners who were granted land were able to exercise

considerable control over activities on their land, including mining and related activities. The passing of the ALRA gave both existing Land Councils statutory powers and responsibilities.

- 11.3 Two additional land councils have been established. In 1978, the Tiwi Land Council (TLC), to represent people of Bathurst and Melville Islands; and in 1991, the Anindilyakwa Land Council (ALC), to represent the people of the Groote Eylandt archipelago was established.
- 11.4 The functions of the Land Councils are set out in section 23 of the ALRA and include:
- ascertaining and expressing the wishes and the opinion of Aboriginals in the area as to the management of Aboriginal land in that area, and as to appropriate legislation concerning the land;
 - protecting the interests of traditional Aboriginal owners of, and other Aboriginals interested in Aboriginal land in the area of the Land Council;
 - assisting Aboriginals claiming to have a traditional land claim to an area of land within the area of the land council in pursuing the claim;
 - consulting with traditional Aboriginal owners of, and other Aboriginals interested in, Aboriginal land in the area of the Land Council with respect to any proposal relating to the use of that land; and
 - assisting Aboriginals in the area of the Land Council to carry out commercial activities (such as resource development, tourism and agriculture).¹
- 11.5 In addition, the Land Councils were required to deliver a variety of services to a range of stakeholders, including traditional owners, other Aboriginals, mining companies and tourists. These services included consulting with traditional owners regarding the use and management of land, arranging for access to Aboriginal land and negotiating arrangements between traditional owners and external parties for land use agreements.²
- 11.6 The audit report noted that the Land Councils faced certain obstacles associated with indigenous service delivery. For example, the services often needed to be provided over large geographical areas, which at times was inaccessible. Their constituents had a low level of literacy and there

1 Auditor-General, *Audit Report No. 28, 2002–2003, Northern Territory Land Councils and the Aboriginals Benefit Account*, Canberra, February 2003, p. 10.

2 Auditor-General, *Audit Report No. 28, 2002–2003*, p. 10.

were often difficulties in contacting traditional land owners who may have been separated from their families or no longer be living on the land under claim.³

- 11.7 In the 1950s, the Commonwealth allowed access to Aboriginal reserves for large-scale mining projects. The statutory royalties paid on minerals produced from Aboriginal reserves were paid into an Aboriginal (Benefits from Mining) Trust Fund. In July 1999, this was renamed the Aboriginals Benefit Account (ABA). It was administered by the Aboriginal and Torres Strait Islander Commission's (ATSIC) Native Title and Land Rights Centre.⁴
- 11.8 The funding available to the Land Councils under ALRA is thus dependent upon the stream of royalty equivalents received by the ABA.
- 11.9 Payments out of the ABA are made under section 64 of the ALRA as follows:
- 40 per cent for administration of the Land Councils;
 - 30 per cent distributed by the Land Councils to Aboriginal organisations in areas affected by mining; and
 - the remaining 30 per cent to be applied at the discretion of the Minister for Immigration and Multicultural and Indigenous Affairs, to be used for:
 - ⇒ payments for the benefit of Aboriginals in the NT;
 - ⇒ extra payments to NT Land Councils administration of the ABA; or
 - ⇒ increasing the equity of the ABA.⁵

The audit

- 11.10 The audit arose from a letter of 21 December 2001 from the Minister for Immigration and Multicultural and Indigenous Affairs, the Hon Philip Ruddock MP, to the Auditor-General in which he requested that an audit of the efficiency and effectiveness of the four NT Land Councils. In a further letter, of 26 January 2002, the Minister asked that the audit include the relevant parts of ATSIC's administration of the ABA.

3 Auditor-General, *Audit Report No. 28, 2002–2003*, p. 11.

4 Auditor-General, *Audit Report No. 28, 2002–2003*, p. 11.

5 Auditor-General, *Audit Report No. 28, 2002–2003*, p. 12.

- 11.11 The objectives of the audit were to assess whether the governance arrangements used by the ATSIC Native Title and Land Rights Centre were appropriate. The audit assessed whether:
- the ATSIC Native Title and Land Rights Centre had met its legislative requirements concerning the ABA in an effective and efficient manner; and
 - the Land Councils are effective and efficient in managing their resources to meet the objectives of the ALRA

Audit findings

- 11.12 The audit found that both ATSIC and the Land Councils had appropriate procedures in place to assist them to comply with relevant legislation.
- 11.13 However, it also found that there was significant scope for all five agencies to improve their performance monitoring and communication with stakeholders.
- 11.14 In the case of the Land Councils, the ANAO found that there was a need to place greater emphasis on outcomes, outputs and cost effectiveness. This would improve the transparency of their operations and allow stakeholders to better assess whether the Land Councils were achieving value for money.
- 11.15 The audit noted that ATSIC could improve the efficient achievement of the functions of the ABA through the development of:
- an explicit objective for the management of ABA equity; and
 - performance indicators for the investments of available moneys.
- 11.16 Performance assessment was a major concern of the audit report's conclusion. The report noted that the lack of adequate systematic performance assessment supported by suitable performance information made it very difficult for the ANAO to assess whether the Land Councils were fulfilling their functions and delivering services in an efficient and effective way.⁶
- 11.17 The lack of performance information meant that the ANAO was unable to assess whether the current level of resources provided to the Land Councils was appropriate. The report noted that performance information such as effectiveness indicators and output indicators would allow the Land Councils to assess criteria such as whether they had produced more

⁶ Auditor-General, *Audit Report No. 28, 2002–2003*, p. 15.

services with the same or lower levels of resources, or increased the quantity of services without any increase in funding. This information would provide a sound basis for funding discussions between the Land Councils, ATSIC and the Minister.

- 11.18 The audit report also suggested the development of service charters as a tool to improve the transparency of Land Council processes and to clarify stakeholder expectations. Land Councils would be able to obtain stakeholder feedback on their performances and to use this information to improve their service delivery.
- 11.19 The ANAO made seven recommendations:
- two were directed at improving ATSIC's management of the ABA and were agreed to by ATSIC;
 - one related to the establishment of audit committees in the ALC and CLC; and
 - four were directed at improving the Land Councils risk management and planning processes and the development of performance information.
- 11.20 The ALC and NLC agreed with all recommendations relating to them. The CLC agreed with all but one recommendation and the TLC agreed with four of the recommendations and agreed with qualifications to two other recommendations.⁷

The Committee's review

- 11.21 On 21 May 2003, the Committee held a public hearing to review the progress made by the relevant agencies in relation to the implementation of the ANAO's recommendations.
- 11.22 Representatives from the ALC, the NLC, the CLC and ATSIC appeared before the Committee. The Tiwi Land Council was unable to attend.
- 11.23 The Committee took evidence on the following issues:
- risk management;
 - collection and use of performance information;
 - development of service charters; and

⁷ Auditor-General, *Audit Report No. 28, 2002–2003*, p. 26–7.

- other issues, including cultural considerations and support for implementation of recommendations.

Risk management

- 11.24 As noted earlier, the audit report examined the service delivery aspect of the Land Councils' work and identified that the Land Councils provided services to a wide range of stakeholders, including:
- traditional owners;
 - other Aboriginals;
 - NT Government departments;
 - Commonwealth Government departments;
 - mining companies;
 - tourists and tourist companies;
 - pastoralists; and
 - commercial and amateur fishermen.
- 11.25 The audit report identified that the Land Councils not only had an obligation of service provision to Aboriginal people as their traditional constituency but that they also had obligations to stakeholders who had purchased their services, for example, providing tourist permits for access to Aboriginal land or gaining decisions on Exploration licence applications.⁸
- 11.26 The audit report noted that the Land Councils were operating in an environment where the risks to effective service delivery were increasing due primarily to the complexity of responsibilities held by the Land Councils.
- 11.27 The ANAO examined the risk assessment and risk management of the four Land Councils and found that there was 'no formal, documented risk assessment to support the strategic planning undertaken by the Land Councils.'⁹
- 11.28 The Committee questioned the land councils about these findings, in particular risk management and the use of audit committees for assessing risk and documenting accountability.

8 Auditor-General, *Audit Report No. 28, 2002–2003*, p. 65.

9 Auditor-General, *Audit Report No. 28, 2002–2003*, p. 68.

11.29 The NLC's response noted that the detailed findings of the ANAO indicated 'good risk management at a project level' and that risk management activities were very much part of the day-to-day work of the NLC. The NLC explained:

It is important for the record to note that we do analyse and manage risks very carefully in relation to all the projects that we do. ANAO were quite complimentary to us in the way we do that at the project level. We acknowledge that that was not formalised into an organisational policy but it was certainly not something we ignored or considered to be unimportant.¹⁰

11.30 The CLC acknowledged that risk management was something that the organisation had not dealt with and that it would be a challenging new area to address:

[Prior to the audit] we had not started working on a documented, strategic risk management process. That is something that, while it might have been around for a few years had not particularly penetrated our organisation. So the challenge for us to do it at ... the strategic level ... as opposed to the project management level, is quite a big one.¹¹

11.31 The Committee also questioned the land councils about the use of audit committees as it would expect to see them in organisations with a sound risk assessment and management framework.

11.32 The CLC declared that it had established such a committee and that the committee had recently held its first meeting. The establishment of the committee had been in direct response to the audit report findings:

... we have been going off the ANAO guidelines for audit committees. The charter will, in the first instance, focus on financial management and oversight and compliance, and then, once we have got the audit committee comfortable with its role, we will move to extend it into risk management.¹²

11.33 The audit report acknowledged that the NLC already operated an audit committee but sought to clarify the roles and responsibilities of such a committee in an organisation the size of the NLC.

11.34 The audit report also acknowledged that the smaller land councils would need less sophisticated risk management frameworks that were

10 Ms Catherine Haire, *Transcript*, 21 May 2003, p. 141.

11 Ms Jayne Weepers, *Transcript*, 21 May 2003, p. 143.

12 Ms Jayne Weepers, *Transcript*, 21 May 2003, p. 142.

appropriate to their size.¹³ It also noted that the TLC had incorporated an audit committee function into an existing committee and recommended this as a course of action for the ALC.

Committee comment

- 11.35 The Committee is pleased to note that all the Land Councils have understood and acted upon the recommendations regarding risk assessment and management and accountability.
- 11.36 The Committee commends the Land Councils for having accepted the advice of the ANAO in a responsive and proactive manner and for having acted quickly to apply the advice to their organisational practices.

Collection and use of performance information

- 11.37 The audit report drew attention to the importance of performance information to an organisation:

Performance information is a tool for management and performance improvement. It identifies where an organisation is heading, whether it is heading in the right direction and whether the organisation is using resources in the most cost effective manner. As well as providing a basis of informed decision making, it is also an early warning system enabling managers to undertake preventative action.¹⁴

- 11.38 The report added that the Land Councils were failing to collect this important information and consequently, the ANAO was unable to accurately assess whether the Land Councils were fulfilling their functions.¹⁵
- 11.39 The ANAO made a comprehensive recommendation about the establishment of an outcomes and outputs framework that also described the need for proper monitoring of performance and efficient use of resources. The report noted that :

The adoption of a performance framework, such as the Commonwealth's outcome and output reporting model, would help the Land Councils to measure their efficiency and effectiveness. It would also improve Land Council reporting and

13 Auditor-General, *Audit Report No. 28, 2002–2003*, p. 65.

14 Auditor-General, *Audit Report No. 28, 2002–2003*, p. 65.

15 Auditor-General, *Audit Report No. 28, 2002–2003*, p. 77.

provide a sound basis for stakeholders to assess Land Council performance over time.¹⁶

- 11.40 The Land Councils, in particular the NLC and the CLC, disagreed with this statement, stating that it was possible to assess performance even when agencies did not conform to the preferred outcome-output framework. The NLC stated :

We acknowledge the fact that we do not currently have the performance outputs and outcomes framework in place within our organisations and because the ANAO prefers that model as a way of assessing effectiveness and efficiency it concluded that it was unable to assess us because we do not use that framework. It is our view that [the ANAO] could have made some comments based on what it saw. It is unfortunate only to be able to assess through the one framework.¹⁷

- 11.41 The ANAO clarified its expectation:

... in any program I would expect to have some performance targets, some statement about your objectives and what you are trying to do, and some measures against that which an external scrutineer ... could follow and make some judgements about performance.¹⁸

- 11.42 At the hearing, however, the Land Councils acknowledged that performance information would be beneficial and agreed that they would be implementing the recommendation in its entirety. The NLC explained that it had undertaken a pilot of the outputs and outcomes framework within one key area of operation and that it was expected this would provide a model for implementation across the organisation.¹⁹

- 11.43 The ALC indicated that it had become aware of the need for greater accountability and performance information through another review in 2001 and that the audit reinforced the learning from the earlier review. The ALC committed itself to continuing the process of reform begun since the earlier review.²⁰

- 11.44 While explaining that some key business areas had sophisticated levels of performance assessment, the CLC acknowledged the lack of a systematic

16 Auditor-General, *Audit Report No. 28, 2002-2003*, p. 84.

17 Ms Catherine Haire, *Transcript*, 21 May 2003, p. 134.

18 Mr John Meert, *Transcript*, 21 May 2003, p. 134.

19 Mr Norman Fry, *Transcript*, 21 May 2003, p. 133.

20 Mr Ross Hebblewhite, *Transcript*, 21 May 2003, p. 135.

approach to the collection and application of performance information within the organisation. It confirmed its commitment to developing and implementing a comprehensive framework that will provide detailed reporting of the CLC's work.²¹

Committee comment

- 11.45 The Committee is pleased that all the Land Councils have agreed to implement the ANAO's recommendation regarding the collection and use of performance information. The Committee considers that the Land Councils have shown a spirit of cooperation that demonstrates sound understanding of the importance of high quality performance assessment.
- 11.46 The Committee also notes that the Land Councils have taken a proactive approach in response to the audit and that the process of implementing the recommendation has begun.

Development of service charters

- 11.47 The audit report commented on the value of service charters:
- All government bodies which provide services directly to the public are required to develop a service charter. The introduction and use of service charters by the Land Councils would demonstrate to their stakeholders that they are committed to providing them with information about the range and standard of services offered.²²
- 11.48 The audit report recommended that the Land Councils develop service charters that included service standards that could be used to assess performance and enhance efficiency.
- 11.49 Three of the Land Councils agreed (the TLC agreed with qualification), however, the CLC disagreed with this recommendation.²³
- 11.50 The Committee questioned the CLC about their reluctance to develop a service charter.
- 11.51 The CLC responded that it would be develop a service charter. It explained that the disagreement over the recommendation had reflected issues of concern held by the CLC regarding the development of such a charter. The CLC elaborated:

21 Ms Jayne Weepers, *Transcript*, 21 May 2003, p. 135.

22 Auditor-General, *Audit Report No. 28, 2002–2003*, p. 87.

23 Auditor-General, *Audit Report No. 28, 2002–2003*, p. 90.

Much of the ANAO's description of stakeholders through the process included traditional owners as stakeholders. We are having what might seem a bit of a semantic argument over the fact that traditional owners are not just stakeholders in the land council; they actually are the land council. We cannot function without their instruction ... But we will implement a service charter. I guess the other aspect of it is that the majority of our council members do not speak English as a first language. Part of what we were questioning was the appropriateness of a service charter which may tick a box in terms of the audit process but will not necessarily make a lot of difference to the land council's responsiveness to the stakeholders—the traditional owners.²⁴

- 11.52 In response the ANAO, while acknowledging the concerns of the CLC, reiterated the purpose of a service charter as a statement or policy that provided some guidelines to stakeholders or recipients of services as to what they could expect from the organisation:

We are saying, 'Put down what people can expect from you in terms of service delivery.' Otherwise, they are going to be complaining about the level of service. They will make their own minds up about their expectations of your agency, which were reflected in some of the comments and criticisms we got.²⁵

- 11.53 The Committee supported the ANAO's view that a useful instrument for agencies to be clear about their role and performance.

Committee comment

- 11.54 The Committee considers service charters to be an important statement which sets out the parameters of an organisation's role and performance. It provides information to stakeholders about what they can expect of a well-performing organisation and, because of this, it serves to focus the organisation on its role and performance.

Other issues

Cultural considerations

- 11.55 The Land Councils gave evidence about cultural considerations that, in their view, were not given enough emphasis in the audit report.

24 Ms Jayne Weepers, *Transcript*, 21 May 2003, p. 136.

25 Mr John Meert, *Transcript*, 21 May 2003, p. 137.

11.56 In particular the NLC expressed concern that due consideration was not given to the efforts of the Land Councils to balance the needs of performance management with sensitivity to cultural factors that impact on the work of the Councils.

11.57 The NLC emphasised that much of the work of the Council had to be undertaken in the dry season, due to the inaccessibility of remote communities during the wet season. However, this caused a clash of priorities, culture and time as the dry season was also the time for ceremony. The NLC elaborated:

We have to ensure that [the Aboriginal people who make up the Land Council] are being serviced in a way that does not conflict with their priorities as traditional Aboriginal people and landowners. We felt that that was not appreciated or could not be picked up in the way that the auditors' methodology looked at it. It is not appreciated just how hard and just what a huge consideration in all of our planning that really is. If we do not do that in a very judicious way, a lot of our work simply would not get done.²⁶

11.58 The Land Councils clearly indicated their willingness to learn from the audit and to implement the recommendations put forward by the ANAO. However, they were also at pains to distinguish the unique circumstances of their relationships with their key stakeholders—the traditional owners of Aboriginal land:

We think the great challenge is on us to show how we can implement these recommendations in a way which is not only meaningful for the parliament when our annual report is tabled but is also meaningful out at Maningrida, Borroloola, Ramingining or Galiwinku, where our key stakeholders live and the people to whom we are, in the first instance, responsible.²⁷

11.59 The Committee recognises this concern and believes the aim of the audit is to assist the Land Councils to improve performance and accountability within their own cultural context.

26 Mr Norman Fry, *Transcript*, 21 May 2003, p. 137.

27 Ms Catherine Haire, *Transcript*, 21 May 2003, p. 145.

Support for implementation of the recommendations

- 11.60 The Committee expressed concern that implementation of the ANAO's recommendations would be an onerous task for the Land Councils, given the current work and resource demands placed upon them.
- 11.61 ATSIC advised the Committee that there was an assistance plan to assist in implementing the recommendations. This included the contracting of a consulting firm to provide the expert assistance. ATSIC noted:
- The minister did offer to provide assistance to the land councils ... recognising that there might not be all the expertise that is required to implement what are fairly complicated processes which public service departments have difficulty dealing with.²⁸
- 11.62 ATSIC emphasised the importance of implementing a consistent framework across the four northern Land Councils, in the best interest of the Land Councils and the Commonwealth.²⁹
- 11.63 The Committee endorses ATSIC's view.

Bob Charles MP
Chairman
17 September 2003

28 Mr Brian Stacey, *Transcript*, 21 May 2003, p. 138.

29 Mr Brian Stacey, *Transcript*, 21 May 2003, pp. 138–9.



Appendix A—Submissions

No.	Individual/Organisation
1	Federal Court of Australia
2	Department of Finance and Administration
3	Department of Defence
4	Department of Defence
5	Department of Finance and Administration
6	Australian Tax Office
7	Department of Finance and Administration
8	Department of Finance and Administration
9	Central Land Council
10	Northern Land Council
11	Department of Transport and Regional Services
12	Australian Taxation Office
13	Department of Aboriginal and Torres Strait Islander Commission
14	Department of Finance and Administration
15	Department of Transport and Regional Services
16	Department of Finance and Administration
17	Department of Finance and Administration
18	Department of Employment and Workplace Relations
19	Australian Taxation Office



Appendix B—Exhibits

No. Individual/Organisation

- 1 Australian Taxation Office
Compliance Program 2002-03
- 2 Australian National Audit Office
Summary of key points: UK accounting manual, Chapter 26
- 3 Sydney Airport Corporation Ltd
Safety & Security Powerpoint Discussion Paper

