



COMMONWEALTH OF AUSTRALIA

Official Committee Hansard

JOINT COMMITTEE OF PUBLIC ACCOUNTS AND
AUDIT

**Reference: Review of Auditor-General's reports first quarter 1999-
2000**

FRIDAY, 3 DECEMBER 1999

CANBERRA

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JOINT COMMITTEE OF PUBLIC ACCOUNTS AND AUDIT

Friday, 3 December 1999

Members: Mr Charles (*Chair*), Mr Kevin Andrews, Mr Brough, Mr Cox, Mr Georgiou, Ms Gillard, Ms Plibersek, Mr St Clair, Mr Somlyay, Mr Tanner and Senators Coonan, Faulkner, Gibson, Hogg, Murray and Watson

Senators and members in attendance: Senators Gibson and Murray and Mr Charles and Mr Cox

Terms of reference for the inquiry:

Review of Auditor-General's reports first quarter 1999-2000

Participants

BARRETT, Mr Pat, Auditor-General, Australian National Audit Office

BURGESS, Mr Trevor, Executive Director, Australian National Audit Office

HAY, Mr Edward, Group Executive Director, Australian National Audit Office

McPHEE, Mr Ian, Deputy Auditor-General, Australian National Audit Office

WATSON, Mr Michael, Group Executive Director, Australian National Audit Office

BASHFORD, Mr Graham, General Manager, Business Development, Centrelink

GAUKROGER, Mr Allan, Chief Financial Officer, Financial Services, Centrelink

WOOLMER, Mr Luke, National Manager, Relationship and Demand Management, Centrelink

COCHRANE, Mr Alistair, Chief Financial Officer, Department of Finance and Administration

PRIOR, Mr Phillip, Manager, Budget Coordination Unit, Department of Finance and Administration

VANNIASINKAM, Mr Homer, Financial Controller, Department of Finance and Administration

CROSSLEY, Mr David, Chief Accountant, Department of the Treasury

McCRAY, Mr Peter, General Manager, Debt Management, Department of the Treasury

**PRESTON-STANLEY, Mr Tony, General Manager, Corporate Services Division,
Department of the Treasury**

**D'ANGELO, Mr Joe, Senior Finance Adviser, Department of the Prime Minister and
Cabinet**

**HENDERSON, Mr Alan, Executive Coordinator, Government and Corporate Group,
Department of the Prime Minister and Cabinet**

**OLIVER, Mr Richard, Assistant Secretary, Corporate Support, Department of the
Prime Minister and Cabinet**

KERWIN, Mr James Roy, Chief Finance Officer, Australian Taxation Office

NEUMANN, Mr Claude, Inspector-General, Department of Defence

**WILLIAMS, Dr Ian Sidney, First Assistant Secretary, Resources and Financial
Programs, Department of Defence**

Committee met at 10.41 a.m.

CHAIRMAN—I will now open today's public hearing, which is the first in a series of hearings to examine reports tabled by the Auditor-General in the financial year 1999-2000. This morning we will be taking evidence on two audit reports, namely *Audit report No. 2 1999-2000—Use of financial information in management reports*, and *Audit report No. 10 1999-2000—Control structures as part of the audits of financial statements of major Commonwealth agencies for the period ended 30 June 1999*. The committee has not received any submissions from agencies in relation to these reports.

We will run today's session in a roundtable format, which means that all relevant participants will be present to hear what others are saying about the Auditor-General's reports. As the content of the reports is linked, the committee will take evidence on both reports in this session. I must ask participants to strictly observe a number of procedural rules. Firstly, only members of the committee can put questions to witnesses if this hearing is to constitute formal proceedings of the parliament and attract parliamentary privilege. If other participants wish to raise issues for discussion, I would ask them to direct their comments to me, and the committee will decide if it wishes to pursue the matter. It will not be possible for participants directly to respond to each other. Secondly, given the length of the program, statements and comments by witnesses should be relevant and succinct. Thirdly, I remind witnesses that the hearings today are legal proceedings of the parliament and warrant the same respect as proceedings of the House itself. The giving of false or misleading evidence is a serious matter and may be regarded as a contempt of parliament.

The evidence given today will be recorded by Hansard and will attract parliamentary privilege.

Fourthly, I remind any members of the press who might be present of the committee's statements about the broadcasting of proceedings. In particular, I draw the media's attention to the need to report fairly and accurately the proceedings of the committee. Copies of the committee statement are available from secretariat staff.

The audit reports being considered in today's session are *Audit report No. 2 1999-2000—Use of financial information in management reports*, and *Audit report No. 10 1999-2000—Control structures as part of the audits of financial statements of major Commonwealth agencies for the period ended 30 June 1999*. I now welcome to today's hearing representatives from the Australian National Audit Office, the Department of Finance and Administration, the Department of Prime Minister and Cabinet, the Department of Trade, the Department of Family and Community Services, the Department of Defence, and the Australian Taxation Office. I thank you all for coming and we will appreciate your input. I suspect that we ought to have your department CEOs here as well, but since we do not we would ask that you at least report back to them what you think you have learned from the kinds of questions that we ask and the sort of response that we expect from all of the departments.

We convened this public hearing to examine the main issues raised in the Auditor-General's reports Nos. 2 and 10 on the use of financial management information and control structures. The JPAA will take evidence today on a number of issues, including the performance management framework and the preparedness for reform. The committee also wants to examine the time frame for implementing adequate control structures.

Does Mr Cochrane from DOFA wish to make a brief opening statement to the committee before we proceed to questions?

Mr Cochrane—No.

CHAIRMAN—Does Mr Henderson from PM&C wish to make a brief opening statement?

Mr Henderson—No, Chairman.

CHAIRMAN—Does Mr Preston-Stanley from Treasury wish to make a brief opening statement?

Mr Preston-Stanley—No, Mr Chairman.

CHAIRMAN—Mr Woolmer from Centrelink, do you wish to make a statement?

Mr Woolmer—No, Mr Chairman.

CHAIRMAN—Mr Neumann from Defence, would you like to make an opening statement?

Mr Neumann—No, Mr Chairman.

CHAIRMAN—Mr Kerwin from the Australian Taxation Office, would you like to make a brief opening statement?

Mr Kerwin—No, Mr Chairman.

CHAIRMAN—Thank you very much. Mr Barrett from the Australian National Audit Office, would you like to make a brief opening statement?

Mr Barrett—I would like my opening statement to be incorporated into Hansard.

CHAIRMAN—Is it the wish of the committee that the document be incorporated in the transcript of evidence? There being no objection, it is so ordered.

The document read as follows—

CHAIRMAN—Where do we start? I read these two audit reports. And as I read some articles in yesterday's *Financial Review*—and accepting that the audit reports relate to some time past—I must admit to a good deal of disquiet and concern, not just about the culture in this change from cash accounting to accrual accounting but seemingly the lack of understanding and implementation of procedures that would allow chief executive officers, and management in general, to make decisions based on information that allows them to manage the business properly. I just say that we have had a look today at better practice guides produced by ANAO—I understand they are on the best seller list, which is good—and at a brief glance it looked like they were pretty applicable.

It just seems to me, having come from the private sector—and perhaps that is a problem when talking to you—that I do not know how you manage a business if you cannot compare the cost of what you do in order to achieve an outcome. For emphasis, I said to Mr Barrett this morning, 'If I were CEO of a department I would like to know what it costs per dollar of benefit to deliver unemployment benefit versus single parent benefit versus age pension benefit versus a Department of Veterans' Affairs benefit.' Would that not be a good control point? Does it not make sense that if each of the department secretaries and line managers understood how much it cost to deliver benefits of one kind versus another kind and if they saw that one was 100 per cent more than the other it would raise alarm bells and they could say, 'What should we be doing that the other department is doing in order to run our business better and provide more benefit for the Commonwealth?'—in other words, more effective use of taxpayers' dollars? That is part of the kinds of things we would like to talk about.

There are a whole range of issues. After these rather negative audit reports perhaps each of you could tell us what it is that you intend to do to improve the financial information provided to managers. We will start with Defence and go around the room.

Dr Williams—I would certainly have to acknowledge that the shift to accruals and outputs is a considerable challenge for Defence. In hindsight, I suspect we have probably started a bit more slowly than we should have done and perhaps that was just a bit of optimism on how quickly one could implement change. At the moment we have a project in place to implement a new accrual financial management system, the so-called Project ROMAN. That is proceeding generally fairly well but there are obviously challenges that emerge. I think that part of the challenge is the point you are getting to, which is that there is a learning aspect—in other words, it is not simply getting the system running but getting managers understanding how to make use of it et cetera.

In our financial statements last year we had a number of concerns raised by the Audit Office and we are planning to address those. We have a meeting of our internal Defence audit committee planned for next week at which we will be addressing a range of issues, not purely systems but management issues. In Defence, unlike many other departments, one of the big challenges is our large asset base—obviously the largest asset holder in the Commonwealth—and that presents perhaps a bigger challenge than for some others who are in many respects still more cash based.

I think the move to accrual accounting has been useful in the sense of giving us some visibility of assets. We are now at the stage where we are in a good cycle of revaluations.

After some challenges in recent years I think we are getting a better feel for the value of our assets and the depreciation flowing from that. There is a lot in train that is working fairly well for us but I do think we have a fairly hard road ahead. The comment I would make though is that from a Defence point of view, as I said, we are very much asset intensive. I guess the nature of business in Defence is in some respects analogous to a research organisation in the sense that we are often chasing the very sharp end, if you like, of the clever electronics or the clever software in order to give us that very fine edge. So at times one has to be careful not to just purely look at the asset in straight economic terms.

I guess what I am saying is that from a Defence point of view the capability aspect is important. I think that is inherent in the processes of government in the sense that it is not merely a financial reporting but also performance. I would suggest that in Defence it is perhaps that performance side which we may do fairly well internally, but I think from a reporting point of view we can do better. So I think we have as many challenges on the performance side as we have on the reporting side.

In summary: we are implementing financial management systems; we have a process in place to do our revaluation on a regular cycle and we are getting better at that; and we are working with the Audit Office to look at the process for valuations. I think there is a challenge to get the senior managers thinking in accrual terms. We have training programs for our SES where we are going out from my division to try and explain to and encourage people. As I said, our audit committee is meeting next week, and the attempt there is to get more visibility. I think that is probably enough of an overview but I would be happy to take any questions.

CHAIRMAN—The Department of Prime Minister and Cabinet.

Mr Henderson—Mr Chairman, the first comment I would make is that I am conscious of the fact that my department is basically in the small league, to say the least, compared to the Department of Defence, the ATO and Centrelink. If we think of accrual accounting mainly from our perspective as focusing on assets—and I know there is more to it than that—the only significant assets we have, now that we have outsourced our IT, are in fact the official establishments of the Lodge and Kirribilli. I must say that the accrual accounting approach to those assets is not really the basis of much questioning in the Senate estimates—most recently the greater focus was on what the Prime Minister gets on his Fox satellite TV. Quite frankly, I would be keen to encourage senators to approach those assets as the national assets that they are, but that is an aside.

Strictly speaking, accrual accounting has not had a major impact on our department, but a lot of the other changes associated with accrual accounting—the greater focus on outputs and outcomes and responsibilities to manage our own cash—have certainly tightened our budgeting approach quite considerably. In that sense there are significant changes for us but, given that we are basically so asset poor, accrual accounting per se has not been a major issue for us.

CHAIRMAN—The Australian Taxation Office.

Mr Kerwin—There are a number of things which have been done within the Australian Taxation Office. I might just go through those fairly quickly. Collectively these things represent a framework which I would believe is pretty consistent with a private sector operation of using accruals and other things. As I go through them I think the picture will start to be painted. I am not starting in any particular place but, in terms of its expense management, the ATO operates an accrual budget. This accrual budget is fully costed with direct costs, internal user charging arrangements, overhead cost allocation and accruals—

CHAIRMAN—Can I just stop you there. You said, ‘full costing’, so you collect time sheet data on what your employees do?

Mr Kerwin—No, we do not.

CHAIRMAN—With respect, how can you sit there and tell us it is fully costed?

Mr Kerwin—Mr Chairman, we had this discussion at an earlier JPAA—

CHAIRMAN—We will have it again.

Mr Kerwin—I think what I said on that occasion still applies—that we are in fact going down the road of having a single time recording system for the tax office. We do have a number of recording systems that are used, particularly around projects, but the area that I am talking about at the moment is just the normal expense budgets. What we have done in relation to those, and not mitigating the need for labour costings, is to rationalise such that we now have hundreds of areas of budgetary control rather than thousands of areas of budgetary control. So the level of budgetary management is now at a much higher level and capable of being linked much closer to outputs than it was in the past. Given that arrangement, we will be able, in the not too distant future—it is on our 1999-2000 program—to have a uniform labour costing system available in the tax office. But at this point in time, you are right; we do not have it, but we do see the need for it.

Mr COX—When you are linking cost items, can you link them to outputs, and is the output revenue?

Mr Kerwin—At this point in time we have linkages on our departmental side through to what we call our ‘outputs’. In the tax office we have four of those, and one is revenue but, in answer to your question, no, we cannot link it to types of revenue yet. Once again, that is where we are shooting for. You will see that the things that I will talk about in the next few minutes are setting a framework in order to let us do that within a reasonable time. But these are the things that I would think need to come into place first—and behaviours around those—to have something that is going to work not only in a systems sense but a behavioural sense within the business.

Mr COX—Okay.

Mr Kerwin—So there is accrual budgeting in place and outputs are costed—I was going to say they are not yet unit costs but I was beaten to the punch on that. On a monthly basis the executive of the tax office gets a balance sheet operating statement, cash flows, Treasury

report and a controllable cost report. In one or two months time there will be a budgeted output type report that also goes to them. When the tax office comes to look at its allocation of resources in any particular period—and we are continually reviewing those things—we have a financial plan in place and we have an understanding of what our balance sheet, operating statement and cash flow positions are going to be for the budget year and three forecast years.

We have put in a financial system and a payroll HR system in order to accommodate some of the things that we need to do in a financial management and recording sense. And we have undertaken widespread training within the organisation around accrual accounting, as well as around the operation of the systems that are facilitating accrual accounting. So I think we have moved a fair way down the track and we do understand some of the urgencies that your questions have pointed to about unit costs.

CHAIRMAN—The Department of Finance and Administration.

Mr Cochrane—In the past year my department has undertaken a huge number of tasks to prepare for the new environment we have now entered. We put in place an accrual accounting system which has been up and running since 1 April ready for the implementation of accrual accounting on 1 July. We have annualised what comes out of the department so that organisational structure is aligned to the outputs that are produced and contains outcomes that we contribute to. We have reviewed our internal control processes and revamped them to meet the new environment. As part of our annual accounts process we got a balance sheet ready for the new environment, so we have a nice clean balance sheet with assets carried forward into the environment and liabilities stated at what we think are the carried values.

At the same time we are the first Commonwealth agency to implement devolved banking in the sense of moving away from the Reserve Bank, and we do our banking with the Commonwealth Bank of Australia. We have also overhauled our total management reporting systems. The whole idea with accrual accounting is that it focuses on three areas: the first is the operating statement profit and loss account; the second is our balance sheet, assets and liabilities—in particular in our case we manage the Commonwealth's property portfolio and on the liabilities side we manage the liabilities through the Commonwealth's super schemes and the various other superannuation schemes; and, thirdly, the cash flow statement which links the operating statement to the balance sheet.

Internally we have done a number of things. We have run a number of courses in accrual accounting—in fact, we issue certificates to people who have completed these courses, and people take that certificate with a pride that they have really achieved something. We have revamped our accounting policies to take account of the new environment—we have brand new accounting policies. When it comes to the future we recognise that to get the true costs of output we need a time recording system, given that a large amount of the business is labour and labour related costs. Whether it is standard costing, actual costing or absorption costing remains to be seen, but the system will be coming in place.

You can see from all of this that there have been a substantial number of projects undertaken in the last 12 months. This does take time. We are changing a culture, and it

takes a good two or three years—maybe more, as identified by the Senate committee which happened in July. But it is important that you lay the groundwork, put the processes in place and have the systems to deliver what you want to achieve at the end of the day.

CHAIRMAN—Thank you. Treasury.

Mr Preston-Stanley—Treasury, I think, has had some similar experiences to other agencies but, in the time since these reports were researched and written, we have moved on reasonably positively. However, there is still quite a long way to go. I think that the alignment of the two major business systems, the accounting system and the HR system, is much closer than it has been in the past, and that has enabled us to better control things like reconciliation processes and so on. I think it will enable us in time to get better links to the outputs and through time recording get much better cost understandings. We are also concentrating a lot now on education, not only with the people who have a direct interface with these systems but also with those who, as managers, have to use the information that they produce. To some extent that is driven by using the development of a better reporting framework, including, as others are doing, regular profit and loss and balance sheet reports to the executive board and making them available in the same structure to the lower level managers. We have also noted some need for better control mechanisms and business rules within that framework, and I think we have made quite a lot of progress on those in the time since these reports have been generated. We are some way from the nirvana that you described, Mr Chairman, but we think we are moving to develop both a framework and an approach which are consistent with getting there.

CHAIRMAN—Thank you for that. Centrelink.

Mr Gaukroger—We have come a long way over the last six months with the implementation of accrual budgeting. We have actually reported accrual budgeting at a top level to our Centrelink board since July 1997, and the budgets we have produced for this current financial year have been devolved down to the unit level for the first time. We have undertaken significant training with the full implementation of accrual budgeting and there have been significant cultural changes with moving about that change from a cash mentality to a full accrual mentality. That is still there, and I think it will take a while to get into the role of a full accrual accounting mentality. The training course is the one issue we have addressed and are continuing to address on an ongoing basis.

The other thing is the ‘walk the talk’ and also ongoing coaching in how it actually applies in practice, because it is one thing to look at the conceptual side of it but it is another thing when we are going through the reality of actually managing those reports. So the reports are being devolved to a unit level on a full accrual basis for the first time. So two significant things are different from the previous system: first of all, there are assets actually appearing in the balance sheet, but having depreciation show in reports for the first time. There has been a great deal of focus on looking at the best way of actually managing assets—do we have too many, do we have too little? Having that focus there has that behavioural effect.

The other area is in leave provisions, and we have had significant issues with actually devolving leave accruals at a unit level. At the top level they are pretty much okay, but at a

unit level we have had some systems issues which we are currently working through to resolve. Having the accruals at a unit level is putting a greater emphasis on managing that leave accrual and the balance sheet, of which we have close to \$300 million. By having it devolved to a unit level and having that accountability for each manager we hope that it will place a greater emphasis on it—for example, taking leave as it falls due rather than letting these things accumulate.

In terms of overall expertise within our finance operations, we have had a number of recruitments over the last six to eight months, one of them being me from a private sector background and my deputy chief financial officer, also from a private sector background. We have also had a number of recruitments, from other areas within the public sector, of highly qualified people who understand accrual accounting. We have ongoing coaching with our current Centrelink staff in financial operations to ensure the full transition to an accrual mentality rather than a cash mentality.

We have had issues with our accrual budgets and we are working on enhancements in the lead-up to the next budget process so that we have it on an accrual-first footing rather than having cash components and accrual components perhaps getting mixed up. We also have in place at the top level a QA process where what we report to the board we QA at the end of the year to see how it matches against the annual financial statements which are on a full accrual basis. I think that is a necessary discipline to ensure that the information that we provide to the board each month really does reflect the expected business result. One of the things that we are incorporating this current financial year is a set of financial statements as a bit of a check against how we are actually travelling—in terms of the information we are reporting each month and where we go for the end of year result. We are also in the process of continually forecasting the year end result, both in terms of the operating result and the cash position. One of the biggest issues we have is making that full transitional from a cultural point of view with all our managers so that they walk the talk.

Mr Bashford—To add to that, we do now collect information on the cost per service per customer within our organisation. We do that by collecting information from three sources. We survey our staff—we have now done three surveys, and are about to enter a fourth, over the last 18-month period. We are going through a re-engineering process whereby we look at every process that we undertake on behalf of our clients—re-engineer it, cost it fully, agree the cost and the price with the client and then collect fortnightly data from the financial and HR systems to check how we are going against those prices. Whilst the system is not entirely accurate, it is certainly accurate enough for us to be able to look at trends and to be able to see the differences between the cost of delivering these various services.

I also add that we put in place some pretty rigid systems in relation to projects, and we do quite a few projects within the organisation. We have to have full business cases before any projects get up. There is a process of determining which of these projects will get up, because there are plenty of requests for these projects. We appoint project managers, get project plans and regularly review the progress of each of those projects. We use timesheets in most of those projects—not fully yet, but we will certainly introduce timesheets for every one of those projects.

CHAIRMAN—Can Centrelink tell us, for instance, the number of complaints per thousand clients in any unit time by type of benefit?

Mr Bashford—I cannot tell you that here at the moment—

CHAIRMAN—Then the answer is no.

Mr Bashford—The Ombudsman would certainly have a lot of that information.

CHAIRMAN—That is not what I asked—I asked if Centrelink could tell us that.

Mr Bashford—I cannot tell you right now, no.

CHAIRMAN—I only asked the question to demonstrate the kind of information that the parliament might consider would be good management practice and the kind of thing that we might reasonably like to know. Just before I ask Mr Barrett to comment on this question, can I also say that, having heard how good your costing system is, we are now likely to ask ANAO to test it for us. Mr Barrett, would you like to comment?

Mr Barrett—Thank you. As always, Mr Chairman, we would take any suggestion from the committee in terms of the audit program. We are constantly testing the systems in agencies, though admittedly more for financial reporting purposes. That has a much narrower context than the one that we have been broadly describing now. So, if we were to look at particular financial systems—as indeed we are looking at the AQIS system at the moment—it is looked at in an organisation-wide context, not in terms of the support it gives the financial reporting or the support it gives to individual managers. As I said to you before, I think that the contextual issue here is obviously getting the information. But there is also the way in which it is used to promote good corporate governance in the organisation, and the leadership that goes with good corporate governance, the extent to which managers actually have information at their fingertips which allows them to manage—and we have just heard of the initiatives which have been taken in Centrelink—and the third element, of course, is the systems themselves.

The issues with the systems themselves are the extent to which they are reasonably robust to generate, say, unit price information, and the focus on getting robust information on an output/outcome basis that is actually user-friendly—and one of the big issues that all of us have had to face is getting information that is user-friendly to people so they actually will use it. Then, of course, there are other issues like the protection of information. The more that we have actually gone away from manual systems and used information technology systems, the more attention we have had to put into the actual protection of the information that is embedded in those systems so that you can give assurance to the parliament, particularly regarding the privacy of individual information, that we are able to ensure that there is actual adequate protection of that information.

So, not surprisingly, when we have gone into agencies and looked at their systems from financial reporting purposes we have seen that there are problems that are created by inadequate or wrong access provisions, wrong use of passwords and so on. We are all still having problems with the sorts of ordinary internal controls that you would expect in a

number of these areas which are integral to the whole issue of financial management. In essence, if I can chance my arm here, for many of us for many years a lot of the risk management and the control environment actually came within the central systems and a lot of us relied on those rather than looking at our own environments. Now that there has been devolution and we are having to have our own systems, it is not just a case of putting in place SAP R/3, Finance 1, OLAS, or whatever the system is. It is a question of whether, from a management point of view, we put proper internal control mechanisms around that and not expect that someone else was going to do it. I think that that is one of the issues in terms of financial reporting and financial information to managers. And from a corporate governance point of view we want to ensure that we have not tossed out the baby and the bath water and that we do have robust control mechanisms which are actually a part of risk management.

The other aspect of the environment that we are talking about is whether agencies are in a better position to actually assess the risks, to prioritise them and then treat them. And this kind of information is absolutely essential now that we have devolved the cash environment and are using our own banking facilities, are having to pay GST and other taxes and charges and use our money to the best advantage. When people around the table are talking about cultural aspects, this is something that they never had to think about and that is why the kinds of programs that we have heard something of this morning are being put in place and are absolutely essential in terms of having available cash, being charged interest and meeting liabilities at particular points in time.

As this committee well knows, the problem in the appropriation system in the past was that even though there have been central controls that have indicated that bills had to be paid within specified periods, there are numerous examples in agencies where in fact that did not occur. Members of parliament, and agencies themselves for many years, have had complaints from the private sector—not just about the core government; a lot of major statutory bodies have had similar kinds of criticism—that we have not paid our bills on time. Of course, there is also the fact that we have not got the payments that were due to the Commonwealth on time. In other words, it was easy for us because there was no associated penalties—the penalty associated was to the budget so we never had to worry about it. But now, of course, this environment has changed and this is the culture, this is the approach and the information essential to top management as part of good governance that they need to ensure that this culture and these changes are taking place in the organisation.

But I think what I hear around this table is that we still have a way to go in actually delivering to the desktop—and it is increasingly the desktop PC of managers—the information that they need not only to manage, but to provide the assurance to executive management that they are in fact meeting their obligations in all the areas that I have tried to explain to you this morning.

So if can put it bluntly, I would not want to see you giving us a hunting licence to go out and start checking on systems per se. What you can be assured of is that in this environment of change as part of our financial statement audits we will take a high profile on their systems and see the extent to which they are delivering the kinds of things that we collectively talked about this morning. But, Mr Chairman, if you were to say to me that because it is an important area of the Public Service the committee would be interested to

look at the costing systems of Centrelink, or any other agency for that matter, of course we would take that into account in our planning for our reports.

CHAIRMAN—Mr Barrett, thank you for that. In Audit Report No. 10, page 17 and 18, under the heading, ‘Accounting systems and controls’ and subheading, ‘Expenditure’, it reads:

Specific matters identified included:

- . the receipt of goods and services not checked prior to payment;
- . payments lacking supporting documentation;
- . delays in acquitting grants and reviewing financial information provided by grantees; and
- . transactions processed by officers without suitable authority.

Then under the heading ‘Cash management and debt collection’ the report reads:

- . receipts not banked promptly and cash advance checks not performed;
- . bank reconciliations not completed in a timely manner or independently checked;
- . invoicing and collection of moneys not timely; and
- . inadequate controls to ensure that all revenue due to the Commonwealth is collected and accurately recorded on the financial systems

One of the things you did not tell us in your audit report is the extent to which these kinds of problems came up. I want to make it clear to everyone here that to the best of my knowledge this committee has never been a whipping boy. We are not here to chastise you, we are here to encourage you. We represent the parliament and we are here to do what we think the parliament would see as better practice so that we go forward. Can you tell us the extent to which these kinds of problems appeared? Is it common, for instance, that invoicing and collection of moneys is not timely?

Mr Barrett—That has been common for a number of years, Mr Chairman. If you do not mind I will actually get the auditors to respond, but from my certain knowledge that has been an ongoing problem for the reason I mentioned to you. I do not know how many times the department of finance worked with agencies to try to ensure that systems were in place to ensure that there was in fact adequate invoicing and collection of moneys. You might be aware that we have done audits into debt collection, which is another aspect of this and which is something that had not received adequate attention for many years. I can assure you that Centrelink and the ATO now have pretty robust systems of debt collection arrangements—

CHAIRMAN—I am glad to know that occurs for the ATO.

Mr Barrett—The fact is that it was not an easy thing, and I think Mr Kerwin can tell you that. In fact, we actually do have an audit in progress now and there is still a problem in this area.

Mr Watson—Those are common threads going through a raft of audits that we have observed. We have tried to summarise them but it is a common theme.

CHAIRMAN—Thank you.

Mr Henderson—Mr Chairman, could I just make a point. You asked Centrelink whether they had data with regard to complaints—

CHAIRMAN—I was just challenging him because he said how great they were doing and I just thought I would find out if they were doing it all.

Mr Henderson—I just want to make the point that the Special Minister of State has just issued a report on the progress in developing client service charters by agencies that have extensive dealings with the community at large. There is a list of, I think, 10 principles in developing client service charters and most agencies now have them. There is an explicit provision in there for feedback reporting mechanisms. I am not across the detail of that but I would have thought that as those client service charter processes are developed there will be systematic reporting in relation to client feedback and complaints. That is an avenue by which the matter you were raising will be addressed much more systematically right across the Commonwealth.

CHAIRMAN—We will keep testing these kinds of issues because, at least in my view, performance management is more than just how many beans are left in the tin at the end of the year. Performance management is about what services a government statutory authority or department provides to the public, how efficiently they are provided and how the public views how well they are provided. I would have thought a scorecard on a chief executive officer of a service delivery department like Centrelink is how well the client base itself views the delivery of those services. That, as much as the cost to deliver the service, is part of the overall evaluation of the management function itself.

Mr Bashford—Mr Chairman, I think you misunderstood what I said. I said I could not provide that information to you here. We in fact collect the information; we have a balanced scorecard. I certainly do not want to give the impression that everything is hunky-dory within Centrelink, but we have moved a long way. There are still lots of things to do but we do run a balanced scorecard which surveys the service we provide to our clients and our customers as well as the financial side of things.

CHAIRMAN—Well, just an anecdotal point from my own office, I have to tell you that you are probably doing better than when it was split up between the CES and the Department of Social Security et cetera, but we still have a substantial client complaint base that comes through members' offices.

Mr Bashford—I would agree with you.

CHAIRMAN—And without counting them I know that is true.

Senator MURRAY—I would like to get this into some kind of perspective from my point of view if I can. It seems to me there are three major questions we all should be asking each other as to whether those answers are now apparent. The first question from the point of view of government, the political executive and the parliament would be: what will we get out of this change? The second question really relates to the agencies and the agency heads, and that is: what will you get out of this change? The third question relates to whether you can do it? Probably the focus today has to be on whether you can do it, but unless you pay attention to the first two questions we have some difficulty. It seems to me from my interaction on numerous committees, and with the senators in particular, that parliamentarians very much are still trying to get to grips themselves with understanding this. It is not just a problem in your agencies; it is a problem in the political world.

My summary of what we would get out of it, or expect to get out of it as representatives of the people, is a more efficient, a more effective, a more competent government, one which delivers a better standard of service and one which adds value to what you are doing at present. But in a sense whilst that matters to you, if you are going to motivate or generate attachment to this process of change it is really what you will get out of it which matters to the people who work for you and the way in which your agencies function. I think that the two elements in there are: what is the utility of what you are doing and what is the benefit of what you are doing? Sometimes the utility is readily apparent—if you can improve the revenue collection process of the ATO it generates obvious benefits in terms of cash flow and security of return and all those sorts of things. But I am not yet convinced that, within the substance of organisations and through the people in your organisations, there is a belief in this process, that they are actually attached to it as something they genuinely desire and see the benefits of. We had an earlier discussion which picked up on some of these points.

I do not think you can change cultures or get attachment or generate commitment unless people do perceive the utility and the benefit to them, their organisations, their lives and their jobs. But if we come to the third question, of which I expect the focus is whether you can do it, in interaction with the Auditor—General and his team we picked on a number of elements. The first is that broad thing called culture. The second is experience—the simple experience or the background—to cope with these changes and the availability of people from the private sector who have an understanding and a background in accrual accounting. The third is the ability—you might have a background but you might not actually have the technical ability. The fourth is literacy, that people use the language in the common and understood way in which they have for years used the cash accounting language and have understood the terminology. Another is responsibility, and that is both widespread right through the organisations but also focused on people—and, lastly, a commitment.

I deliberately packaged up an approach in that area because I read the Vertigan report which came out yesterday—I doubt that many of you have had the opportunity yet to look at it—and I am familiar with these documents and so on. For me the real question arising out of this is to hear from you—because this is going to be a lengthy process: I think the Auditor-General has clearly indicated years, and Mr Vertigan went as far as seven years in some respects—whether you are getting your organisations to a stage where they believe that they will get something out of it, right through the organisation. Secondly, which is behind

the chairman's remarks to Centrelink, can you do it in a time frame which is respectable, and really that will be a judgment of the parliament as to whether you are getting along with it in enough speed and with enough efficiency. So in the responses to specific questions I would like a reaction and some sort of response to the remarks I have made.

CHAIRMAN—Could we go around the table in order again.

Mr Neumann—I might handle some of the questions and then I might ask Dr Williams to talk about some others. I will take the third part of your question first, Senator, if that is all right: can we do it? The answer is yes, but I think the issue here is time and money. Some of the logistic systems in Defence will take several years and tens of millions of dollars to fix. As Dr Williams has said, we are already trying to put in place a new financial system and also a new personnel system. On your first two questions—

Senator MURRAY—Sorry, can I interrupt as we go. Have you worked out a time frame in which you think this can happen reasonably, because, given the nature of your problems, I would expect Defence to have a quite different time frame to PM&C?

Mr Neumann—The time frame for the financial system and the personnel systems have already started and they are probably a couple of years away from full implementation. But with the logistic systems all we are doing is trying to cobble together three separate systems for each service into one system. In COMSARM, for example—the explosives ordinance inventory system—the initial stages, where we have one system rather than three separate systems, I think will be about April 2000, but that will not be the end of it; the systems will need further improvement in order to do the sorts of things that the chairman was talking about.

In terms of what the agency will get out of it and what the government will get out of it, in some cases I think they are the same things. For example, if I take obsolete stock—we have a large amount in Defence and the removal of the overheads associated with it is quite important; I think we had about a billion dollars worth of obsolete stock—the process is starting on that too. But again that will take time because there are hundreds of thousands of line items in certain cases. So I think it is a question of effort, commitment, if you like, and at the end of the day also funding.

In terms of commitment, I think that has increased in Defence. I think if you went back two years there probably was very little commitment but I think there has been a substantial increase since then, certainly at the senior levels. At the more junior levels, though, where you have people who are used to ticking and flicking manual systems, I think it is going to be a hard call quite frankly, particularly if people are of the age group where they are thinking about retirement—it is very hard to get commitment to change at the end of working careers.

Dr Williams—I have a few comments to add. Just getting back to your three questions, I will start with the first one: what will the parliament get out of it? We are certainly trying to work through our PBS statement and our PAES statements to give the parliament a better feel for the performance. I suspect that perhaps on the resource side—at least from a cash

basis, and hopefully in time on an accrual basis—we give a reasonable degree of visibility, but I think on the performance side we have probably not done as well as we could.

One of the things that I think accrual accounting is doing for us is giving us a better visibility, or at least more management pressure to look after our asset base. I would have to admit that some years ago, if the question were asked how many missiles of a particular type we had, we actually had great difficulty answering that because they were spread around—some were on ships, some were wherever. I think what accrual accounting has done for us is say that we have to be able to account for those assets. So I would hope that we will, from the parliament's point of view, be able to give better visibility of our assets and give better performance measurement. We are very much in a transition on the output approach, but I think it also gives us the opportunity to give parliament a better feel for what we are actually providing—rather than broad statements we can relate it to specific outputs.

In terms of the department, I would agree with Mr Neumann's comments that there is probably a growing acceptance at the higher levels, but I still think we have a long way to go. I still think people are thinking in cash terms. At the very low levels where people are actually day to day dealing with accrual, again I think they are managing it reasonably well. Probably the mass of people in the middle are the area we need to try and push.

Just as a final point in terms of your time frames, we are looking to have our Project Roman for the financial management system, or at least the major components of it, in place by the end of this financial year. There are some areas we already recognise as challenges—the introduction of GST is obviously one area we now have to pick up and move with, and some of the budgeting is not as good as it would like to be and we need to develop some modules. On our personnel systems, at the moment they really are picking up the payment of salaries in most instances and what we need to do is develop and pull together our civilian and the three military areas into a single system which has the full accrual, leave et cetera factored into that.

So we are progressing but there is still a way to go. To pick up Mr Neumann's comment again, it will take money and it will take time, and in the interim there is a fair bit of handrauc work to pick up some of the accrual aspects of our accounting.

Mr Neumann—If I could just add one thing. The ultimate end of this, I think from the Defence point of view and from the government point of view, is greater combat capability. I think that would be the shorthand way of saying that.

Mr Henderson—Senator Murray, the answer to your question, from PM&C's perspective, depends a little on the scope of your question. With accrual accounting, strictly speaking in terms of the management of the department there are not substantial impacts—as I said before—but we were one of the few agencies in this report to get an unqualified report on our financial statements. We have implemented new software systems for finance and for HR and the responsibility for managing our own cash certainly is tightening up our budgeting. So there are significant changes there but I would not describe them as dramatic.

If we define the reforms more broadly to introduce enterprise bargaining, the development of more robust performance indicators for outcomes and outputs, and if we take into

account the impact of market testing and the development of client service charters, then, yes, there are very significant changes under way in our organisation. We are trying to bring some of those changes together by integrating our individual performance agreements, which are now developed under our certified agreement for all staff, and to an increasing extent relate the contents of those individual agreements to the performance indicators for individual work units, divisions and the department as a whole. Over time I think that will have a significant impact on the way we operate.

In terms of the department's external clients, overwhelmingly of course they are the Prime Minister, his office, and the cabinet, so we do not have a client service charter as such but we are developing them for our own corporate services people. In that sense we are developing client service charters for the corporate services we provide in-house on the same basis as we have service level agreements with the corporate services that we have outsourced. We have outsourced all our payroll functions and our accounts processing functions, plus a number of other smaller corporate support activities.

In 1998 we market tested the whole corporate support function in our department—there would have been 70 or 80 jobs covered by that. The outcome was that in fact the private sector only offered us significant savings for those two activities that I mentioned, so we downsized by about 20 or 22 staff in the finish. Basically, if you are considering the whole sweep of public sector reforms that have been introduced, yes, I think over a period of three or four years you are going to observe very significant changes, but, as I said before, from a financial point of view accrual accounting is not a dramatic development for our department.

Senator MURRAY—What I am searching for in the answers, and you have provided that indication, is that in my view accrual accounting is the financial way of establishing value—in other words, applying a value system right throughout the organisation—and unless people start to understand that it remains a job of finance officers or people who are attuned to accounting and IT systems. But really what it means is attributing value to every aspect of the organisation and reflecting it through financial statements. I do not know if you would agree with that summary, Auditor-General, but that is my view of it and that is why it very much has to be a total organisation approach. That is just an observation.

Mr Kerwin—In relation to the parliament, what I would hope the parliament would get from these sorts of reforms would be a much better informed view about how the business was being conducted. If the business was conducted on the basis of cash balances they could have been categorised in a whole variety of ways but basically it is still cash balances. In relation to the accrual world that we are in now, an accrual measurement system, and within the accounting construct of balance sheeting operating statement cash flows, cash is just simply one line item in a balance sheet. Nowadays there are basically the assets of the organisation, the liabilities of the organisation and, with interpretation, an equity position that comes out of the balance sheet. In relation to assets, it will be very important for public sector businesses to consider whether they should be in the fixed asset ownership business or not. Because, in relation to what we do as part of our business, we do not operate fixed assets per se—we might need them but we do not necessarily get the return on them that a business that exists for the simple purpose of owning and operating fixed assets would have.

So it will cause us to examine our balance sheet on the asset side and it will definitely cause us to examine our balance sheet on the liability side, particularly around liabilities that have accumulated over some period of time and will accumulate into the future. In relation to our cash position, we will need to make sure that we remain solvent. So, in terms of the information that is available on an annual basis, and through the Department of Finance and Administration on a monthly basis, parliamentarians and the parliament as a whole should get views of how these public sector businesses are operating.

The other thing that the parliament should particularly get from our organisation is a timely delivery of the various reforms that we are involved in at the moment and within a cost context that at the end of the day—and I will use GST as an example; the unit cost of, say, delivering GST into the states—is one that the states would find reasonably acceptable. That means that when we are doing our project work around delivery of these we do have an eye to what the operating cost of a GST system might be and to what the operating cost of an Australian Business Number system might be. So there are levels of sophistication in our thinking coming through our project management, or what we call our investments, that this framework is certainly assisting and facilitating.

The cultural aspects of that, and the behavioural changes from a cash world and a functionally-driven world to one where there is accrual measurement—which captures most of the things that we call ‘costs’ and has a focus in terms of what in fact you are doing, not what you have capability to do—are starting to come into our organisation. Just mentioned briefly before was the debt position. Our agency agreement has payments under it for a number of key performance indicators, if delivered. If those things are not delivered then certain payments just do not occur under the agency agreement.

On the other side of the coin we have a culture which is developing in our business which basically says that the things that we do and the accrual framework will help us do this one way; the things that we do will actually help us grow the business. The things that we do in terms of this notion of growing does not necessarily mean getting bigger for whatever ends. It means that in terms of viewing how we do various things government will select us to continue to do those things.

In terms of the individual, the individual is involved in that, although the social contract between public servants and their organisations has probably changed nowadays from what it may have been, say, a decade ago. There was long-term employment for security and there were trade-offs and there was some level of social contract that had built up over time—now we are in a world where those sorts of social contracts are probably breaking down. In order to accommodate that change, which is quite a significant change, we are developing this notion that our destiny is really in our hands and our delivery of outputs at lower costs and within time frames that people are looking for them to be delivered in, are the things that are going to assist us in remaining viable and interesting to the government and the parliament.

Senator MURRAY—I did not really get a good impression from Defence, but, from the perspective of your agency, and in view of the criticisms by the Auditor-General and by Dr Vertigan of how we are going with this process: do you have a time frame established by which the process will be largely complete?

Mr Kerwin—In terms of the end game, I would think another 12 to 18 months.

Senator MURRAY—As quickly as that?

Mr Kerwin—Yes, in relation to the financial reforms operating with reasonable levels of sign-on by people, because we have already moved down the track, as I described before. We certainly have systems in place which are capable of doing these things. For instance, we produce a balance sheet operating statement for the administered side of the business, which is the revenue of the Commonwealth side of the business, and our departmental side. On both of those we do that within 14 days of the end of every month—we have our budget reports available within four to five days of the end of every month. We have these things distributed. The behavioural aspects of those are the ones that we are still working on.

We have a particular approach to investments which is pretty consistent with what Centrelink was talking about. There needs to be project initiation briefs, cases put forward, and we track the benefits. So if somebody says, 'These are the benefits from this investment,' we track them to see whether they are in fact delivered, and that is part of performance management. So I would say that in 12 to 18 months those sorts of things will be in place and operating in a behavioural sense.

CHAIRMAN—Does that 12 to 18 months include accurate operating costing systems, Mr Kerwin?

Mr Kerwin—Yes, it will. In the Taxation Office at the moment we have a number of time recording systems which are built out of a range of things. In 1999-2000 we will look to have a uniform SAP based time recording system—which is the product that we are using in conjunction with a number of other things.

Senator MURRAY—Can you just remind me what SAP is?

Mr Kerwin—It is just a vendor of financial and other products.

Senator MURRAY—What does it stand for?

Mr Prior—It is a German company.

Mr Kerwin—Yes, the largest in the world.

CHAIRMAN—Another acronym.

Mr Kerwin—Another three-letter acronym for you, yes.

Senator MURRAY—I will lighten the mood by telling you that the other day a senator told me that in the midst of a hearing on trade matters one of the people said, 'When I was talking to Osaka the other week something happened,' and apparently one of the members of the committee said, 'Hold it right there, what's Osaka an acronym for?'

Mr Cochrane—I think you have covered the main issues, Senator. I would like to answer from a slightly different perspective in the sense that I have been involved in reforms in another jurisdiction which took a number of years to perform and so I have the benefit of what we can expect to get out of this. More importantly, the first one is that there will be a much better understanding of what each department does, and this comes back to the value of money concept. The point was made earlier that there is a lot of focus on the financial reforms and that accrual accounting is in fact only the framework which allows you better management—you build your blocks on top of that, and in some cases you can build them or decide not to in other cases. It will certainly enable a much better view of the performance of the organisation and the non-financial section of the PBS—these are key performance indicators and each department has to record them and include them in their annual report. That will definitely give senators and members a good feel for what has actually happened in the organisation.

Part of all this is education. There has to be a willingness of senators and members to learn about the new system, to be able to come to understand financial concepts, because as an accountant I spent years of training to understand and implement them. It does not happen overnight, and there comes an important aspect: the reforms should not basically lie on the accountant's desk; it is the manager's job to manage and accountants to give them the information. The big cultural change is that managers are going to have to pick up these skills and apply them.

CHAIRMAN—Are you recommending a training course for us?

Mr Cochrane—In a word, yes. I think the results of this will be much better financial management and accountability in the agencies, and this does take a number of years. In my experience the best thing out of all of these reforms will be improved decision making and much more data and information to allow better decisions.

Senator MURRAY—Let me just stop you there. We are early into the process. Is the nature of the change already resulting in changes in the advice and perspective you are offering to government?

Mr Cochrane—I would say it is too early for that because I think the reforms are staged: stage one is the implementation of the reforms: get things up and running and then get them bedded down.

Senator MURRAY—When do you think it will materially start to—

Mr Cochrane—I would believe in the next financial year, as we review what has happened.

Senator MURRAY—In 2000-2001?

Mr Cochrane—Yes, but that is just my opinion.

Senator MURRAY—So the government will not see the physical benefits until then?

Mr Cochrane—There could be examples of seeing benefits, yes, but do not forget that the PBS for this year was set pre-accrual without actually experiencing how it is going to operate in the live environment. There is a time lag there, that is what I am trying to say.

Senator MURRAY—Do you share Mr Kerwin's view and think that DOFA can get across all this within the 12- to 18-month period?

Mr Cochrane—I think it is going to take longer.

Senator MURRAY—For your department?

Mr Cochrane—Again, it is staged, but to have everything in place, up and running, managed with full accountability regimes in place and getting the full benefits is definitely a three to five year time scale.

Senator MURRAY—Are you talking whole of government or are you talking DOFA?

Mr Cochrane—I would say in general whole of government.

Senator MURRAY—And for DOFA itself?

Mr Cochrane—Probably three years.

Senator MURRAY—Why would you be much longer than the ATO?

Mr Cochrane—As I said, I have experience of having done this before. The Vertigan report suggests five to seven years; I would say three to five years based on my experiences.

Mr COX—That is for DOFA, but what about for line departments who are probably less enthusiastic?

Mr Cochrane—I am actually answering as a line department in this instance.

Senator MURRAY—Are you suggesting Mr Kerwin might be being a little optimistic?

Mr Cochrane—I actually do not know too much about the ins and outs of the ATO—it might be quite simple to implement, so it is possible. I would just say that based on my experiences, 18 months is relatively—

Senator MURRAY—I am not being mischievous with this, but it would be apparent to everyone around the table, and to the committee, that for an organisation like Defence there are going to be a very different range of problems—and some intractable issues, I would think—which might incline for a longer time period. But the fact is whoever leads sets the standard for the rest and the parliament and the government obviously will want this to get up and kicking as early as possible. That is why a time frame is relevant, because if Dr Vertigan is saying this thing could take seven years it would be inappropriate to have a judgment of seven years across-the-board if for some agencies it is 12 to 18 months and others it is seven years. Then you start to get a perspective as to how to deal with individual

departments rather than taking a generalised whole of government view, which I think was the point of the chairman's question to you earlier as to whether those particular issues in your report were generic or specific. That is why I am testing the time frame issue.

Mr Cochrane—I think the time frame depends a lot on the commitment of the department and it is up to the department and ministers to determine the speed for the department to actually get the results. If the commitment is there then it can get done in a shorter time frame.

Mr Neumann—Could I just add to that slightly. It also depends on what the departments are doing. For example, we are running through the defence reform program at the moment. We have had a commercial support program running since 1991 and I think we have tested something like 10,500 positions and 94 separate activities. This is another element, and Dr Williams mentioned the GST which we have to pick up as well. This is another element on top of everything else that has to be managed. But, Senator, if I could just say that, whichever method you use—and we are using accrual accounting because that is what is set down at the moment—there are benefits in having full cost exposure, because managers suddenly realise the full cost of what they are doing rather than just the additional cost or the net cost, which is what they have been used to operating on in essentially a cash basis.

The problem with the cash basis is that people just say that what you got last year is what you obviously need the following year without thinking through all the implications of that. There are some conceptual benefits and there are some actual benefits and I think some of them are going to be delivered reasonably quickly. I cannot speak for other departments because they have different things, but even in Defence itself we are getting a better concept of the value for money through several reform processes, and the benefits are there in terms of investing that in greater combat capability already. This will be just another stage, if you like, in the whole process of becoming more efficient and effective.

Mr Barrett—I share all those sentiments that have just been expressed. Just to give you an example, in the last piece of data we had there were 27 agencies on SAP R/3, which is therefore the most popular accounting system that is being put in place at the moment. Now, without exception major agencies are having trouble implementing that particular financial system—I do not think anybody is going to say differently. However, the Public Service Commission office have had no problems with implementing SAP R/3. Why are they different? Because they are a simple organisation with simple requirements, and this is bringing out Senator Murray's point about the earlier question. Whether or not we think that the PSMPC should have gone to the trouble and expense of having SAP R/3 is another issue, but clearly there are differences of the kind I just mentioned.

For instance, I have recently heard the secretary of the Department of Employment, Work Place Relations and Small Business make the comment that already they are up to something like 70 something patches in the SAP R/3 system and still going. That is timely, it is costly, and it is not delivering the functionality to his agency that is required, so Alistair is right in the sense that there are horses for courses here. But I think the general view is that agencies are going to take some time to get some of these systems in place to meet the requirements of their agencies. That comes back to Senator Murray's point about the credibility and the usefulness to the individuals at all levels of the organisation, because no-one is

going to own any of that stuff if in fact they do not understand it or they are not getting credible delivery of information to actually make a difference to the way in which they take decisions or do their business.

So I would be a bit inclined to be in the DOFA camp in terms of the time for medium to large agencies. The problems for small agencies are quite different, not just in accordance with the example I gave you of the relatively simple requirements of an organisation like the Public Service Commission, but clearly in terms of their capability, their resources and the resources they can attract. When I refer to the resources they can attract, I am talking about the specialist resources they can attract to do the job—and then the actual money. I can assure you from our point of view that the investment we are having to make in these systems is pretty significant, and is in fact making a difference to our cost of audits. We are looking at this very critically on a value for money basis. But there is a bind here, because we have moved into the system of accrual accounting and accrual budgeting and an outputs and outcomes basis. In essence, short of someone actually getting out and devising a particular system that best meets our needs, we have no choice but to actually take one of the packages that have been up on the list in order to be able to deliver the requirements of this new system.

So there may indeed be a lack of ownership in the first instance because no-one actually had to say, 'What is it we actually want to do ourselves as an organisation and what is the best system of doing so?' The fact is that there was a decision taken, we moved and we had to in fact meet the requirements. Unless it could be shown that we could more cost effectively take up a different system to the half a dozen or so packages that are on the list, that was the way in which it went.

In essence, there are agencies that have reservations—or certainly have problems—about the extent to which their initial expectations on whether such systems would meet public sector requirements have in fact been met. That is the reason that there is a shared responsibility for the timing and the efficacy of these new systems, because in the normal course of events anyone who has anything to do with implementation of systems will know that until you actually have to implement the system you do not know the problems that you face. I think that now a number of them are facing problems that they did not necessarily envisage they would have to.

CHAIRMAN—When you say this, Mr Barrett, are you talking about the problem of the accounting package itself—that is, the software system that is running—or is it more to do with lack of expertise within the individual departments in order to be able to manage it?

Mr Barrett—They are two of the explanations, Mr Chairman, but what I am suggesting is that it is not just agencies' deficiencies, if you want to describe them that way. The fact of the matter is that we do know that packages like SAP R/3 were designed for the private sector—they were not designed for the public sector—and there are changes that have had to be made to those packages. To give an example, I have heard that in order to make immediate use out of the facility of SAP R/3 some agencies have actually used the tax sections of that package to provide the capability required. Of course, now they are going to have to operate a GST so I do not know what the heck they are going to do, to be frank. In a sense they are going to have to go back and open that capability up to allow them to use

the taxation elements of SAP R/3 and then they are going to have to go and do something else to put in the capability they put in the tax element.

CHAIRMAN—Is there no agency that internally designed a system, or went outside and hired consultants to design a system? It is not like the government said on 30 June, ‘Oh, by the way, on 1 July you will now move to an accrual accounting system.’ That is not what happened; there was one hell of a lot of lead time. Are you telling me that not one single agency designed an accounting system?

Mr Barrett—I am not aware of any agency that has designed an accounting system. For the most part that was the whole reason for the then Office of Government Information Technology going out on behalf of all of us to the industry to actually get packages that best met the perceived requirements of the public sector. We were then invited to use whichever one of those packages that best met our particular needs, with the proviso that if we were able to identify a package out there that was not on that list and that was more cost-effective we could in fact make a case for that to be used.

CHAIRMAN—Perhaps I am wrong, but I would have thought that the needs of a capital intensive department like Defence, which also has huge operating costs, versus an almost total labour cost operation like PM&C, were so diverse that there would be no possibility of having a standard accounting package that would work for both.

Mr Barrett—You have Defence that use SAP R/3 and you have Centrelink that use SAP R/3. To be frank with you, the intelligence coming from the private sector in recent years has been that you do better, given the costs associated with developing these systems, going the package route and if you do not get 100 per cent of your requirements, you only get 90 per cent of your requirements, that is still the way to go. It was much more cost effective to go the package route and if you absolutely had to develop additional capability then you looked at that quite critically as to its cost effectiveness.

CHAIRMAN—So you are saying that the advice pretty uniformly was go the way that departments have gone?

Mr Barrett—I would be interested in my colleague’s comments, but that certainly would be my view.

CHAIRMAN—Are you now critical of that advice?

Mr Barrett—No, I am not critical, I am simply trying to give you the reasons—that it is not just a case of agencies and their culture or their expertise that is a stumbling block or will take time. I am saying that the nature of the packages themselves and what has to be done in order to get them to do the kind of work that is necessary is a factor which we cannot ignore.

Senator MURRAY—Just a question on that line of questioning. I assume you have the option within the package to adapt it; I assume you are not required to keep it entirely as it was. Let us use your example and assume the package was 90 per cent effective but you

needed that extra 10 per cent. In terms of the adaptation process, does that have a time frame attached to it as well? How long does that take?

Mr Barrett—It can, Senator. There are two things that you need to be aware of here. The first is the general experience of most of us that any adaptations to packages are pretty resource-intensive and expensive, so you do not do it lightly. In fact, most of us look at our systems and what we do and try to re-engineer those as best we can to minimise patches or adaptations—or whatever other description you want to make—of computing packages. That of itself takes time to actually look at the implications of changing the way you do your business in order to minimise the necessity for making expensive changes to computing packages.

Senator MURRAY—But give me a specific example. You gave the DEWRSB example of 70 patches; is that the total number of patches they need and over what period did they do that?

Mr Barrett—In their case I would imagine over a number of months. I dare say they did it because they absolutely had to in order to make the system work to meet their requirements. We have Finance 1 in our organisation but in the corporate area we have had quite a lot of work being done—far greater than we estimated, and it is still in process—to ensure that the package actually provides not only the management reports but the capability of delivering in a whole range of financial information and financial management areas.

Mr COX—I want to tackle a different line of questioning. As the report on control structures goes through department by department we find that there is a lack of adequate reconciliation between departmental FMIS systems and DOFA's FIRM system and there is a lack of qualified accrual accounting staff in line departments. Who actually knows what is going on financially within line departments: do line departments or DOFA?

Mr Prior—With regard to the first part of your question, can I say that FIRM is no longer a system that is used. In the move to accrual accounting FIRM is officially dead, we do not use it. I do not know if any agencies use it—the auditors might know. So that is kind of an ancient history if you like. The second part of your question was to do with qualified persons in line agencies. DOFA does not monitor who is qualified and who is not in agencies, but in our dealings with agencies we would support the Auditor-General's report and the particular points where he makes that comment. I think that is a very, very important point to make. As Senator Murray was saying before, this whole accounting, accrual et cetera reform is not about a clerical exercise. It is actually the strategic aspects of it that I think the government is looking for. If it is seen as a clerical exercise it is just debits and credits instead of debits.

Mr COX—But who does know what is going on in particular departments? Is it DOFA or is it the line department?

Mr Prior—Knows what is going on in what sense?

Mr COX—In a financial sense.

Mr Prior—DOFA has access to the budget estimates of all departments. DOFA now collects monthly financial information from all departments and produces consolidated financial statements, and they are currently producing those quarterly. DOFA also produces the annual consolidated financial statements of the Commonwealth. So in that sense DOFA has a view of that financial information, but if your question is about who is qualified, what is the skill level and how is it managed et cetera, there is a devolved process that has been introduced. DOFA has a role to play but much of the financial management has been devolved in this reform.

Mr COX—So how confident are you of the quality of the budget estimates?

Mr Prior—DOFA has a number of quality assurance processes in place. They involve things such as memorandums of understanding, risk assessments and so on of agencies to gain assurance about the quality of the estimates coming forward, as well as having our own quality assurance and quality control processes at DOFA. So we are very confident about the quality of the estimates that have come forward.

Mr COX—The Vertigan report says that there is very little accrual accounting information in the finance greens that go to ERC. What is the reason for that?

Mr Prior—I would have to see that particular line in context to understand exactly what Vertigan was trying to say.

Mr COX—Perhaps somebody who might have been in ERC could enlighten us as to whether there is much discussion of accrual information in the budget process?

Mr Henderson—Mr Cox, you appear to be looking at me. Unfortunately, I have not been to ERC in the last few years.

Mr COX—There are a few issues that we probably should go through here since we are considering reports that relate to particular agencies and some deficiencies in their activities. In the control structures report for Treasury there are a couple of concerning aspects. It says:

It was also noted that reconciliations between the Public Debt Management System (where Commonwealth debt is recorded) and the general ledger were not completed for the first eight months of the year. Such reconciliations are the key control in the timely detection and correction of errors.

Can Treasury enlighten us as to why they did not do reconciliations between the public debt management system and the general ledger?

Mr McCray—The simple answer is that there were problems with implementation of the general ledger system, which meant that the information was not available to do the reconciliation for the first eight months of the year. As soon as the information became available, in February-March, the reconciliation was undertaken. Subsequently, the Audit Office acknowledged in its correspondence with the department that it was our standard practice to do these reconciliations.

Mr COX—Why was the information not available for so long?

Mr Preston-Stanley—This is a consequence of bringing the new, in our case SAP R/3, financial system into play and possibly an inadequate supply of professionally qualified people in the organisation. We also had a restructure early in the financial year which meant that we had to go back and remap the data set inside the financial system.

Mr COX—What sort of risk do you think the control systems were put at over the course of that time when they were not being adequately monitored?

Mr Preston-Stanley—I do not have a good sense for the extent of the risk there.

Mr McCray—There have been a number of independent reviews of the debt management control framework which have found the framework to be sound and consistent with good industry practice. That gives us a reasonable degree of assurance that the framework itself is fundamentally sound.

Mr COX—Can you tell us a little bit about the Auditor-General's other concerns relating to Treasury's derivative credit risk policy?

Mr McCray—Are you talking about the single policy document?

Mr COX—Yes.

CHAIRMAN—It is on page 56 of Audit Report No. 10.

Mr McCray—I would not want to understate the significance of that as an issue, but what we are talking about here is the fact that we have a substantive credit risk policy document, which is approved by the Treasurer periodically. Since that last major review of the credit policy there have been a number of minor adjustments to it. We have also prepared a manual which documents the process for operating the computer software that we use to calculate credit exposures. So there is in the credit policy itself, some very minor operational adjustments to the way we conduct our swap transactions and the addition of a manual on the operations of the computer software. So we have three documents maintained in a single folder. When we come to next review the credit policy there will be no difficulty in simply merging those three documents into one.

Mr COX—What sort of derivatives are you presently using?

Mr McCray—Interest rate swaps and currency swaps.

Mr COX—And they have not changed in character over the last four or five years?

Mr McCray—We have been using currency swaps for 11 years now and they have not changed in character. We have only been using interest rate swaps since August 1997 and they have not changed over that period.

Mr COX—Can you tell us a little bit about the interest rate swaps, how it is managed?

Mr McCray—The credit risk or the process in general?

Mr COX—The actual process of doing the swaps first.

Mr McCray—I suppose that the purpose is a logical place to start. We seek purposefully to manage the interest rate exposure of the cumulative debt portfolio. The debt portfolio's interest rate exposure is not just a product of what debt we issue, but rather we issue debt in particular parts of the yield curve to achieve particular objectives. We then use interest rate swaps to manage the interest rate exposure in line with a target—a benchmark target as we call it—which is one recommended by external consultants. In essence, over the last couple of years we have been swapping fixed rate exposure for floating rate exposure to shorten the duration, or the interest rate exposure, of the portfolio.

I think it is fair to say that our approach in terms of process is more rigorous than market norms in the sense that we ring around and get bids from three or four people in the market as to where their swap prices are on that particular day and we choose the best bid, or if two bids are equivalent we will use some other criteria, such as how much credit we have used with one counter party versus another. That contrasts with market practice where that multiple bid process is not used. The credit policy that governs our relationship with counter parties has been thoroughly reviewed in relatively recent times by the Audit Office, and by Arthur Andersen on behalf of the Audit Office, as follows:

Arthur Anderson concluded that credit risk is well managed by Treasury and the practices adopted are toward the upper end of industry practice.

Mr COX—Is that a published report?

Mr McCray—Yes, it is.

Mr COX—Can we get a copy of that?

Mr McCray—Sure. So there is both the physical process by which we conduct our swaps, the bidding process I am referring to, and the credit policy that governs the relationship of individual counter parties in terms of our swap transactions. We are pretty confident that is rigorous and, as the report indicated, in line with best practice.

Mr COX—Can you tell us what sort of exposure you would have to swaps?

Mr McCray—Well, the swap book would be of the order of \$20 billion worth of swaps but, of course, we are swapping cash flows so it is not an exposure in that sense. The market exposure of the swap book varies from time to time but it is not a trading portfolio, we are not using swaps to try and pick movements in interest rates and make money. So in a sense the trading value of the portfolio is not that useful an indicator. We think that the most useful indicator of the value of our swap activities is their longer term performance in reducing debt service costs, which they certainly have done over the years.

Mr COX—The other issue that I think we probably ought to raise with Defence is on page 30 of the same report. It says:

access controls over the explosive ordnance inventory system (COMSARM) are less than desirable. The lack of segregation of duties over user access, creation of access and program changes represent the greatest risks to unauthorised access or changes;

Can you give us an indication of what sorts of risk the Commonwealth might be exposed to by people misusing the ordnance inventory system?

Mr Neumann—I think that pricing data risk is the key issue there and that should be fixed when, as I explained before, the system becomes one in April 2000. In the meantime what we use is an off-system manual checking to verify the accuracy of quantities and values. That is essentially how it is managed at the moment.

Mr COX—There is no great risk of diversion of materials?

Mr Neumann—I should not have thought so on that particular system but I would need to check that.

CHAIRMAN—Are we in any danger of somebody walking off with a Mark 9 torpedo?

Mr Neumann—Because of the size of the Mark 8 torpedo—or the Mark 48 actually—probably not, but we do have other issues about explosive ordnance and firearms. We have in place a system of audits done by my internal auditors of defence establishments and usually at unit level, which is the small holdings, there is not an issue. There is an issue, however, at some of the central depots and we have measures in place. For example, one of the depots now has an armed guard on it whereas before it did not. We now track firearms by serial number whereas before it was not always done.

Mr COX—They used to get moved around in bulk?

Mr Neumann—As I understand it, what tended to happen is they were tracked by serial number when it got to the units, and they were quite good at it, but when we sent stuff off for disposal and when there were bulk movements people just boxed them, and that was the problem. We also have a small problem that sometimes duplicate serial numbers were issued from the manufacturer.

Mr COX—Were there any issues of firearms vanishing when they were sent off for disposal?

Mr Neumann—There have been allegations to that effect, and because of the records it is very difficult to establish the accuracy of those claims.

Mr COX—None of them have turned up in a subsequent murder investigation?

Mr Neumann—Not to my knowledge—it does not mean they have not been used.

CHAIRMAN—I am advised that Senator Murray's questions have not been answered by Centrelink.

Mr Gaukroger—There are several topics I would like to cover on where we are travelling within the framework of accrual budgeting. The first point is the systems; the second point is the presentation of focus; the third one is using financial and non-financial information together; cultural issues; and then the efficiency dividend return to government. With the financial systems we actually have systems that are in place and operating on a full accrual footing, but that is not to say that we have not had implementation problems, for example, I mentioned earlier the issue of leave provisions and trying to devolve those to a unit level. We have had significant issues with getting numbers that make sense at the unit level, although we have it at the top level, but we had some initial problems there as well. For example, on a monthly basis we have accruals coming through for things like salaries, we have depreciation charts coming through and the change in leave provisions.

The second point is the presentation of focus. We have a number of things in train at the moment for further improving our own budgeting process. For example, under our current budgets we have cash salaries and accrual actually separated as line items. I think a key driver with moving to a full accrual footing with the cultural changes is the presentation. We are combining those and there is just one thing called ‘salaries’, because they are one and the same when you are looking at matching your expenses to revenue over a 12-month period.

The simplicity side of it is all-important too in helping our people understand these reports and ensuring that the presentation is simple to understand to enable use of those reports. We are looking at changes there. The separation of capital and expense budgets, and having two separate budgets for our managers in the next financial period as well, is another change which we are undertaking. We got to the financial and non-financial measures because the financial measures are just one part of looking after how one manages a business. It is about managing the various trade-offs with the business and looking at financials and non-financials.

Examples of non-financials might be the staff numbers or the business volumes and one of the biggest changes with moving into an accrual environment is how instant it is, for example, changes in customer numbers. For example, under the old cash environment essentially we had 12 months to make any decisions on changes with our staff numbers; under the accrual environment we have to be a lot more rigorous in improving our forecasting tools much further over the hill with things like changes in customer numbers so that we can anticipate it. When you are looking at what the benefit might be for both Centrelink and the government, it is greater anticipating those workload changes, making adjustments at the end of the day and being able to reduce the cost of providing the services.

The cultural change, I think, is one of our most significant ones because of the sheer size of Centrelink—we have 22,000 employees nationally across Australia. We have made some inroads into that with training, coaching and the like. But I think it needs to be recognised that we are talking about a major cultural shift from cash to accrual, and having systems that think and talk accrual, having presentation and walking the talk that is all accrual, I think, is a major area of working through that cultural change. At the end of the day we have an obligation to return an efficiency dividend to government under an accrual environment. It presents a framework where expenses are matched to the revenue, and under the cash environment you have things that can slip in either way between years. Under accrual

accounting there is a much greater chance of showing what the true financial position is of an organisation. As I say, we have done that the past two years with returning the efficiency dividend to government and we are working towards the same this year.

Mr Preston-Stanley—I have to own up to not answering the question either. I do not have much to add in terms of the generality of the issues that have been raised. As we have just made obvious, Treasury did have some difficulties in introducing a new financial system in the last financial year. It was partly because of the system, partly because of the people issue. That was exacerbated also, particularly in the accounting area, by a lot of turbulence in turnover in the staff at that work level. On the cultural issue, and similarly the experience issue, we have actually gone out and recruited some people, including the gentlemen on my right from the private sector with a strong accounting background and experience in an accrual environment.

Like PM&C, we are much more a people-intensive agency than an asset-based agency. So there is a fair concentration on getting the systems that underpin the decisions and the information that relates to both our people costs and our accrued liabilities associated with people, as well as addressing some of the issues about asset management and better capital management rules. The cultural one is actually similar in Treasury to a number of other places but I would just like to raise one more. Some of the people in HR, for example, have to think of themselves much more as people who are dealing with significant resource issues. In turn, they are working with an information system which draws to the attention of the managers things that they have not been experienced with before. It is amazing how focussed our attention becomes when you point out that the people that they have working for them not only cost an annual salary but carry a significant accrued liability, which is continuing the issue that Mr Gaukroger mentioned before about taking leave when it accrues and that sort of thing.

So that is all part of a significant cultural issue that, internally, you would expect to achieve out of this better internal management, better understanding of your own decisions and those of others. Similarly to others, we are working on developing a better reporting framework. We have been trying to concentrate on developing a report framework based on the P&L and so on—the balance sheet—at the executive board level, which will feed down structurally to all other management levels so that there is a common system and a common set of indicators of financial performance. They become more detailed, of course, as you get lower down in the system.

There is another issue on the system that the Auditor-General was mentioning with the patches and so on. I think there has been a bit of a mutual issue there about not only we purchasers of a new financial management system understanding what we are buying, but the vendors and the people who assist them in bringing them into the agencies understanding the environment that they have brought that system into. I think, at least for Treasury, we are now on a better mutual basis than we were and I would be confident that a lot of people would get confidence in what is being produced by these systems. I think that will be quite an important issue because otherwise you still have the debate, not about what this system is telling you but about the difference between the handraulic system that somebody has been used to and adapted along the way and what ought to be a system of record. So there is another cultural adjustment issue there.

On your question about timing, Senator Murray, I would not like to be pinned to it but I would be thinking that this is more a matter of years rather than a year. I would have said 18 months to two years in terms of better financial and general management information, a little bit longer maybe to get firm connections from your initial budget and estimating process right through to your outputs and outcomes.

Senator MURRAY—Mr Chairman, having listened to those responses and the interchange between, if we refer back to the *Use of financial information in management reports* from the Auditor-General there are a couple of things in his recommendations that I was picking up on and listening for. The first is the critical path recommendation which is really the time frame. I think we have a good feeling as to where that is going. The other one was really the recommendation concerning the establishment of financial objectives. Hearing the responses around the table, I am clear in my own mind that literacy in this area is still not apparent, even at this level, in the sense that there is not a common language movement, if I may say so. What I mean by that is I hear still an attachment to the old language. We talk ‘cost effective’ rather than ‘benefit effective’; we talk about ‘efficiency dividends’ rather than ‘value dividends’—‘value dividend’ is not a term that is commonly heard but it refers to my earlier remarks that I believe the real benefit of this process is the delivery of greater value overall.

I make those remarks, Mr Chairman, really to indicate an expectation, as a member of this committee, that the financial objectives which would be established as a result of the Auditor-General’s recommendations, and which I would hope the agencies would follow, would in fact reflect a perspective of where the agencies are going and what they would get out of it; rather than the kind of functionality approach which I think has been the problem with past methods, and is still apparent in the language we use. It is not a criticism of the people on that side of the table because it is a criticism of the people on this side of the table as well. We have great difficulties in shifting perspective and movement.

CHAIRMAN—Does anybody have any comments?

Mr Barrett—Mr Chairman, Senator Murray would not be surprised that I agree with what he is saying, and it actually accords with the outputs/outcomes framework. The only thing I would say—which is the common message that we are trying to get without it being misunderstood or twisted in the translation—is that it still takes good process to get good outcomes. I was making the point earlier about the presence of centralised controls and centralised agencies who had responsibility for particular aspects of the resources and their use which they do not have any more in a devolved environment. Where there might have been adequate control measures—and I put that question mark—the fact of the matter is that now it is an issue for all of us in our own environments that we do have robust control mechanisms, because at the end of the day they will actually determine the credibility of the information that is provided on which good outcomes are being achieved. So what I am saying is, yes, use terms like ‘benefit effective’, but I would not like to see us lose the ‘cost effective’.

Senator MURRAY—No, it is the balancing up.

Mr Barrett—Yes.

CHAIRMAN—I have two small questions left but before I finish up on this topic I would like, on behalf of the committee, to thank everybody here for a degree of frankness that is not always apparent between, if you will, the bureaucracy and parliamentary committees. We have tried over some substantial period of time—and Defence knows this well—to get a degree of reality into these things and that, in a sense, is described by what we think about when we think about risk management. We talk about risk management. That means we expect you to take risks, which means we expect you to fail from time to time. That is what risk management is all about—it is about taking risks in real life, which means failure is inevitable.

I do not think that we are here to beat you over the head every time something goes wrong. Sure, it needs to be pointed out and, yes, the lessons need to be learned, but if people come in and sledge, and people come in and obfuscate, and pretend that everything is wonderful and the sun is bright on the horizon and there are no storm clouds, and nothing is ever going to go wrong, then we will never move forward. So, from my viewpoint and our committee's viewpoint, it is better that we can be reasonably open and honest with each other. So I thank you for that.

I have a simple question. A number of you have talked about hiring outside accountant consultants to help you in your control work and your computer systems and imputation work. Has anyone thought of or has anyone tried hiring any engineers to do costing work for you? No. That is really interesting. Well, may I say to you that you might think about it because engineers are bloody good at costing. Having said that, Mr Cox has another question.

Mr Barrett—Can I make a comment? I know why you are asking, but in essence I think you will find that the people with that kind of experience are indeed working in a number of the consultants' firms that we do employ. At the end of the day what we depend on is that they make the best selection of people who can actually help us do our jobs, in essence, rather than us going and trying to put our fingers on particular people in that respect. Obviously when we go out to recruit, as we have done, you can see even in this room that there is a variety of experience that is brought to the Public Service from outside recruitment, but in terms of the use of consultants, I do not know that there is a whole range of experience out there that is brought to bear to help agencies.

CHAIRMAN—Mr Barrett, notwithstanding your statement I will stick with my recommendations.

Mr COX—I have a couple of sets of questions and the first lot is to Mr Cochrane. You said that you came from another jurisdiction that had gone through the process of implementing an accrual budgeting system; which jurisdiction was it?

Mr Cochrane—The New Zealand government.

Mr COX—What was the quality of the budget estimates before they started doing accrual budgeting?

Mr Cochrane—I think, like any other jurisdiction in the world, they were cash-based. The whole focus there now is on accrual accounting. Parliamentarians, in my opinion, have a much better understanding of what each of the departments is delivering and it is represented through the parliamentary select committee process which really questions what is being achieved in each of the departments. That took a number of years to achieve.

Mr COX—But in terms of the actual accuracy of the estimates that the New Zealand Treasury were publishing before they moved to accrual, were there problems for several years and they were all over the place?

Mr Cochrane—As far as New Zealand is concerned, I would say that with the improvement of accrual accounting the quality of the estimates improved remarkably.

Mr COX—Instantly or it took a while?

Mr Cochrane—It took a while.

Mr COX—How long?

Mr Cochrane—Three to five years.

Mr COX—Do you anticipate the same sort of problem happening here—that it will take a few years before they really settle down?

Mr Cochrane—I would say that this year after budget night when the economists had a look at the estimates they agreed with what we said the surplus was going to be, so one can only draw the conclusion that the budget estimates on an accrual basis first up were very accurate.

Mr COX—So you think that they will be as accurate this year as the mid-year review says they are going to be.

Mr Cochrane—I would not really like to comment on that.

CHAIRMAN—Can I ask ANAO one last question and then we will close down. What are the consequences for the government's fiscal outcomes of failing to implement effective control structures within a reasonable time frame—and I am specifically referring to Defence's earlier statement regarding the accuracy of their asset base?

Mr Watson—Can you repeat the question.

CHAIRMAN—What are the consequences for the government's fiscal outcomes of failing to implement effective control structures within a reasonable time frame? For example, I go back to what Defence said and what you said to us at an earlier time. If we keep revaluing assets because we got them wrong and taking huge write-downs, what are the implications for the overall fiscal outcomes of the government's budget strategy?

Mr Barrett—I will take that to start off with, Mr Chairman. I was going to ask Michael to respond because of the Defence implications and representing 70 per cent of the whole of government outcome. Of course, with the numbers that we were talking about earlier, those kind of revaluations, or establishment of assets that were not found previously are other issues that come up in that respect. Clearly, you are going to have a marked income on fiscal outcomes and therefore the confidence that was just mentioned by Mr Cochrane in terms of the estimates will clearly be an issue. The point is that we need to get that degree of confidence as soon as we can, particularly where the big numbers are concerned. It is a self-evident truth. If there are conceptual problems, if there are methodology problems, if there are systems problems that create variations of those kind of orders that we indicated, then clearly the credibility of the government's fiscal balance is at issue. That is why we are saying that there has to be good control mechanisms, to give the government and the parliament the confidence that those numbers are not going to be moving from year to year in ways that give credence to the fact that we do not have control over the estimates.

Mr Prior—Mr Chairman, could I make a comment in response to Mr Barrett's comments. The government's primary fiscal targets—and I am sure my Treasury colleagues could confirm this—are, as stated by the Treasurer, fiscal balance. As my colleagues at Treasury would understand, and perhaps Mr Barrett does not quite yet appreciate, fiscal balance does not include revaluations and devaluations of assets; they are written back.

Mr Barrett—We understand that fully, but it nevertheless does not take away from the fact that where there are large variations which will become evident in the near future they have to be sorted out so that there is credibility.

Senator MURRAY—One last question from me on a practical area. Has the switch to accrual accounting and the consequent accrued liabilities provisions for employees affected at all the perception as to recruitment or movement of staff from one agency to another? Has it in any way clogged up that system or has it had no effect at all? Does anyone have a view on that?

Mr Kerwin—I think it is fairly early days in relation to our businesses in this federal Public Service, but I might just reflect back on a little bit of experience in local government. In local government these sorts of movements have been going on for years, and in reality it did not affect selections per se, because I think there was an understanding that on balance sometimes you would win and sometimes you would lose. This is within the transfers and cash following the transfers.

Mr COX—I would like to ask the tax office whether they could throw any general light on the Auditor-General's concerns about the integrity of control systems in relation to fraudulent activities, particularly data corruption and breaches of confidentiality.

Mr Kerwin—In terms of data corruption, and if I can go to the question of access controls which I think you are talking about, since the report there have been a number of things which have changed and which audit will have a look at when they come around next time. In principle, what has changed is that we have work area administrators who allow accesses to occur. That was the case as in the past. Those administrators probably have a better what is called 'matrix' of accesses with respect to particular jobs that people do to

make sure that the access is somewhat related to the work that people need to do and for the time that they are doing that work.

Probably the major change that has occurred is that we now have a central area which has the job of being an independent review over those accesses, and we look for the work area administrators to provide a report at least once every three months on what is there and a confirmation that it is still there as a consistent link or a necessary link between access and work. In the event that those reports do not arrive, there is follow-up by this independent group. That is sort of control that has come in.

In relation to confidentiality, in the tax office for quite some time there have been categories of clients who have particular indicators on their electronic files which mean that if anyone goes near them there is a very solid audit trail back to whoever looked at it. That audit trail will go back to the particular user who needs certain identification in order to do these things. There is a full monitoring of those things half-yearly.

In relation to another issue that we have had in place for some time, we have a continual education or an awareness program around ethics and around the absolute necessity for confidentiality of taxpayer/client files. The particular approach that we are following currently is not to hand out rules—although we do have a national policy on this sort of thing. It is a little bit more experiential in that we actually get people together and facilitate understandings and conversation around just vague things that might be pointing people in the direction of compromising themselves in relating to looking at records when they do not really need to look at records.

In relation to the actual altering and corruption of data, I do not know of any evidence in relation to that. I suspect that you would see evidence if there was widespread abuse. I do not believe that is the case. In relation to client accounts, certainly in the areas where we have these categories in place the review on those would pick up any examination of those. Our internal audit also conducts a program using a tool that can search in order to look at who has been gaining access to particular client accounts.

Mr COX—Okay, thanks.

CHAIRMAN—Gentlemen, thank you. It has been a good public hearing but at the same time I think perhaps it has acted as a kind of a conference, if you will, between departments in a sense to hear each other talk about problems, shared experiences, individual expectations of how long it will take to get wherever it is each of you wish to go. In that sense I hope it has been useful for you as well as for us. Thank you for coming and thank you for helping us come to grips with these important issues.

Resolved (on motion by **Mr Cox**):

That this committee authorises publication, including publication on the parliamentary database, of the proof transcript of the evidence given before it at public hearing this day.

Committee adjourned at 1.00 p.m.

